TimberWest

maintaining our FOCUS

GROWING GREATEST VALUE THROUGH OPERATIONS EXCELLENCE

2003 ANNUAL REPORT

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CONTENTS

2003 FINANCIAL HIGHLIGHTS

	2003	2002	2001	2000	1999[1]
Operations *(in millions of dollars)*					
Net sales	**$ 428.5**	$ 464.9	$ 461.9	$ 487.0	$ 456.6
Operating earnings	**58.7**	99.3	87.2	96.2	90.5
EBITDA[2]	**70.3**	101.9	100.6	109.1	80.2
Earnings available for distribution[2] before provision for future income taxes and write-down of property, plant and equipment and related costs	**42.2**	65.8	58.8	68.0	63.1
Distributable cash[2]	**51.4**	90.1	83.5	89.2	83.3
Per Stapled Unit *(in dollars)*					
Basic and diluted earnings available for distribution before provision for future income taxes and write-down of property, plant and equipment and related costs	**$ 0.55**	$ 0.88	$ 0.90	$ 1.02	$ 0.91
Basic distributable cash	**0.67**	1.21	1.29	1.34	1.20
Diluted distributable cash	**0.67**	1.20	1.29	1.34	1.20
Distributions paid	**1.08**	1.08	1.08	1.08	1.08
Financial Position *(in millions of dollars)*					
Net working capital *(excludes short-term borrowings and distributions payable)*	**$ 40.6**	$ 56.3	$ 50.4	$ 37.1	$ 48.0
Total assets	**1,440.9**	1,478.3	1,487.2	1,505.3	1,529.5
Total debt	**255.0**	236.5	378.6	375.1	342.0
Unitholders' equity	**875.5**	914.8	788.5	787.7	673.9
Total capitalization[3]	**1,130.5**	1,151.3	1,167.1	1,162.8	1,015.9
Debt to total capitalization	**22.6%**	20.5%	32.4%	32.3%	33.7%
Market capitalization *(at December 31)*	**968.3**	914.3	841.0	703.4	661.3

DISTRIBUTABLE CASH

Distributable cash includes consolidated earnings before income taxes less cash income taxes, plus depreciation, depletion and amortization, plus proceeds from the sale of property, plant and equipment net of their gain (loss) on sale, less additions to property, plant and equipment and, from time to time, adjustments for other items deemed appropriate by the Board of Directors.

[1] Information presented for 1999 has been restated to reflect the retroactive effect of a mandatory change in methods of accounting for income taxes and employee future benefits for fiscal years beginning on or after January 1, 2000.

[2] EBITDA, earnings available for distribution and distributable cash, are measures that do not have a standardized meaning prescribed by Canadian generally accepted accounting principles (GAAP) and may not be comparable to similar measures presented by other companies. Reconciliations between net earnings, as determined in accordance with GAAP, and these measures are included within the management's discussion and analysis contained in this annual report.

[3] Total capitalization is equal to total debt plus unitholders' equity.

OUR ASSETS

TimberWest Forest Corp. is the largest owner of private forest lands in Western Canada and is unique in that most of its log production is sold on the open market, which provides considerable flexibility to meet market opportunities. The sale of logs accounts for about 80% of the Company's revenue. The Company's private timberlands include about 6,000 hectares of properties that are being progressively made available for higher-value uses.

TIMBERWEST OPERATIONS

PRIVATE LANDS

- 334,000 hectares, mostly located on Vancouver Island. The majority of sites support forests of Douglas fir, a premium species used for structural purposes.
- TW applies rigorous environmental and conservation practices for wildlife and water quality protection and a wide range of other conservation goals.

PUBLIC LANDS

- two renewable and long-term public Tree Farm Licences.
- provide the right to harvest 1.3 million m^3 of logs per year.

SECOND-GROWTH HARVESTING

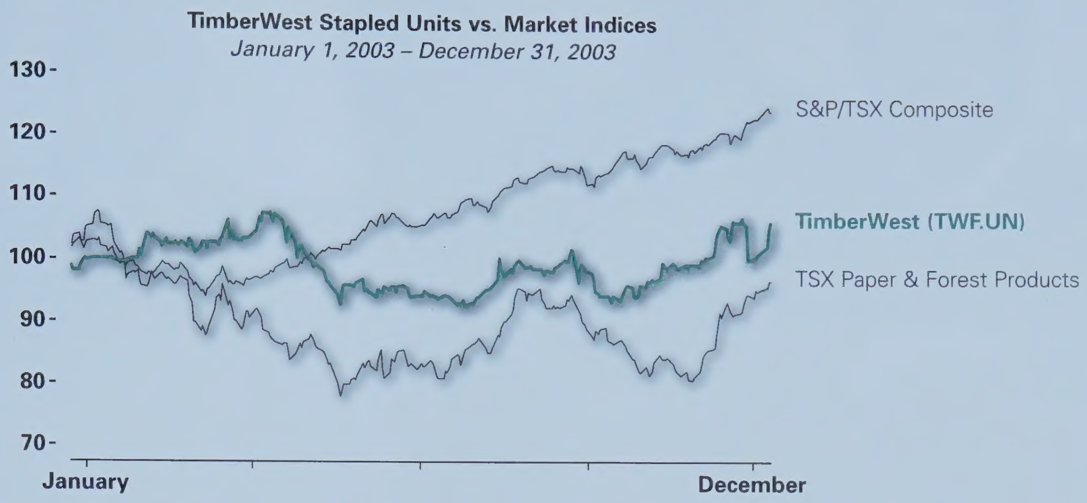
- about 60% of TW's harvest on both its private and public land is second growth.

CERTIFICATION

- third party auditors, KPMG Performance Registrar Inc., have certified that TW, on its private forest land, conforms to the objectives and performance measures of the American Forest and Paper Association's Sustainable Forestry Initiative (SFI®). The TW lands certified support a long-term (50 years) harvest of 2.3 million m^3 per year. The annual harvest level is reviewed by TW every five years to ensure its sustainability.
- KPMG Performance Registrar Inc.'s third party audits have determined that all of TW's operations and facilities have environmental management systems that meet the requirements and standards for ISO 14001 international certification.

LUMBERMILL

- TW operates a lumbermill at Elk Falls capable of consuming 900,000 m^3 of logs annually.



OUR VISION

GROWING GREATEST VALUE THROUGH OPERATIONS EXCELLENCE

MAINTAINING OUR FOCUS

From the CEO

FINANCIAL RESULTS COMMENTARY

The year 2003 is best described as the "Perfect Storm" for those operating in the coastal forest industry of British Columbia. In the opinion of most long-time participants, conditions were the worst ever.

Log and lumber revenues were adversely affected by three major events. Markets were oversupplied at home and abroad, the Canadian dollar appreciated at an unprecedented pace relative to its US counterpart, and the Canada/US softwood lumber dispute continued unresolved for another year. Some 80% of TimberWest's operating revenues are log sales and, relative to 2002, the average external log sales realization declined 10% in the year, resulting in a $38 million decline in revenues related to log sales. While about half of this variance is attributable to currency, the balance is related to weaker markets and a lower-value species and end-use sort mix.

Costs and production levels were also negatively affected in 2003 by a stumpage system on Crown land that was not market based, logging curtailments imposed by the driest summer operating season in more than 60 years of record keeping, and a coast-wide strike by the IWA that took all logging and most sawmilling operations down for more than a month near the end of the year.

At TimberWest, capital spending in 2003 was also $13 million above normal levels because of strategic investments to upgrade our Elk Falls Lumbermill and to acquire real estate for the construction of a new log sort yard on Vancouver Island. Distributable cash was reduced by a corresponding amount.

The effect of all the foregoing was that TimberWest's distributable cash for the year ended December 31, 2003, was a disappointing $51.4 million on sales of $428.5 million. In 2002, the Company generated $90.1 million of distributable cash on sales of $464.9 million.

Cash flow from operations, after changes in working capital, was a more positive story in 2003 because considerable working capital was turned into cash in the fourth quarter. As a result, debt levels are still modest at $255 million, although $18.5 million higher than at the beginning of the year.

The Company paid out $82.1 million in distributions to its unitholders in 2003 and had to borrow to satisfy some of this requirement.

While TimberWest harvested 2.5 million m^3 of logs from its private forest lands during the year, it only harvested half its annual allowable cut on Crown lands because of problems with the coastal stumpage system.

It was a trying year for our Elk Falls Lumbermill as well, which produced a more costly mix of products in an environment where prices were declining across the board. Two of Elk's main objectives for 2003 were to complete the installation of new drying kilns and to have the mill up and running on three shifts by mid-year. Although it was successful in meeting both, it had to curtail operations beginning in July and it incurred 10 weeks of downtime for the year.

▲ **Left to right:**

President and CEO Paul McElligott

Vice-President of Strategic Planning and Forest Policy Hamish Kerr

Director Conrad Pinette

Director Robert Murdoch

General Manager of Manufacturing Ed Vervynck

OPERATIONS EXCELLENCE

While 2003 delivered a number of setbacks caused by events the Company had no direct control over, real gains were realized with all major elements of our Operations Excellence strategy, including cost reductions and enhanced safety and forest management.

COST-REDUCTION PROGRAM

All operations continued to work hard on reducing costs and improving productivity in 2003 and, despite the tough operating conditions, our private land operations made good progress against their cost reduction targets, achieving a \$4.27 per m^3 improvement over 2002 costs of production. These gains were offset by difficulties at our public land logging and sawmilling operations, which were unable to achieve their targets due to the low level of operations during the year. As a result, Timberland Operations achieved a \$0.99 per m^3 improvement in costs over those for 2002 against the Company's target of \$4.50 per m^3 for 2003.

SAFETY

We also made good progress on our safety performance in 2003, a core component of our Operations Excellence strategy. At Elk Falls, we achieved a MIR of 2.56, bettering our target of 4.0 and our 2002 MIR of 4.1. Timberland Operations achieved a MIR of 4.48, narrowly missing 2003's target of 4.3 and improving on 2002's MIR by 18%. In addition, the number of days lost was reduced by 63% and the severity rating for 2003 showed a reduction of 54% from the previous year. Employees and contractors performed admirably, and we intend to continue building on what was accomplished in 2003 and work safer in 2004.

ENHANCING VALUES

TimberWest is committed to maximizing the value of its forest estate. Part of this will be through investments in silviculture, enhanced forest inventory information systems, and improved capability to model the growth and yield of our tree farm. This will, in turn, allow us to increase the long run sustainable yield on our private lands. We worked aggressively in these areas in 2003 and our first accomplishment has been to increase the genetic worth of Douglas fir seedlings planted from an average of 5% in 2003/04 to an expected 11% in 2005. The percent gain refers to the expected wood volume increase at harvest over using wild seed. We are also moving to a regime of two rounds of fertilization on selected sites and improved site preparation for plantings. Field measurements are also expected to confirm in 2004 that our plantations are reaching a height of two metres earlier than assumed in our yield tables. All of this is to say that we expect to be able to confirm an increase in our long run sustainable yield in the year 2004.

MARKET EXPANSION & TRADE

In 2003, 60% of our log sales volumes were within BC, 22% went to Asia, and the remaining 18% to the United States. Private land log exports continue to be a critical part of our success because, like any business, we want to diversify our markets and ensure we are realizing the highest value for our products. The premium earned by selling private land logs at international prices also allows TimberWest to harvest stands that would otherwise be uneconomic. This is what has enabled us to continue operating profitably on private land and keep employees working at a time when most Crown timber–dependent companies were curtailed.

Unfortunately, we are still hindered in our efforts to achieve the best value for our resource by the federal government's Notice 102, which restricts the sale of BC logs outside of Canada. We remain optimistic that Notice 102 will be rescinded as part of a settlement of the Canada/US softwood lumber dispute. We also believe that any negotiated settlement must include quota for new entrants as part of any transitional arrangement to free trade. Having invested $9.5 million in new capital and added a third shift, our Elk Falls sawmill is very much a new entrant requiring market access.

STEWARDSHIP

In 2003, TimberWest continued its commitment to fostering sustainable forest management, maintaining water quality for domestic use and fishery values, mitigating environmental risk, and protecting key public environmental values and private timberland assets.

We obtained ISO 14001 certification for the newly constructed North Island Dryland Sort, so all of TimberWest's Timberland Operations and facilities' environmental management systems, including Flying Tankers Inc., are certified under ISO 14001. The Company's private timberlands are also certified under SFI.

We continued our close collaboration with Ducks Unlimited, the Marmot Recovery Foundation, the Nature Conservancy of Canada and Pacific Salmon Foundation. We also sold a 171 ha site to The Nature Trust of British Columbia and made a donation of more than $200,000 to help protect high-priority fish habitat on the Englishman River.

KEY INITIATIVES & ISSUES

Sale of TFL 46

TimberWest initiated an auction process for the sale of TFL 46 and associated forest licences in September, and signed definitive agreements with the Teal-Jones Group for the sale in early 2004. This sale is subject to several conditions, but it is expected to close during the first half of 2004.

We are pleased with this transaction as it greatly simplifies our business model and it allows us to pursue our strategic objective of increasing our focus on the private timberland portion of our business.

Private forest land regulation

Following two years of work between private forest landowners, including TimberWest, and the provincial government, the BC legislature passed the results-based

▾ Left to right:

Vice-President of Log Marketing and Sales John Kelvin

Vice-President of Public Affairs and Government Relations Virginia Aulin

Director William Brown

Assistant Vice-President of Timberland Operations Gerry Young

Director Kenneth Shields

Average Annual Investment Returns

Asset Class	1993–2002 (10 yrs.)	1983–2002 (20 yrs.)	1973–2002 (30 yrs.)	1960–2002 (43 yrs.)
Timberland*	10.0%	12.3%	14.5%	12.6%
Commercial Real Estate	9.3%	7.7%	9.5%	9.3%
S&P 500	9.3%	12.7%	10.7%	10.1%
US T-Bills	4.4%	5.7%	6.6%	5.8%
US Consumer Price Index	2.5%	3.2%	5.0%	4.3%

* Measured as the holding period returns from a portfolio of US timberland. Source: Hancock Timber Resource Group (2003)

Private Managed Forest Land Act in November. The passing of this Act, which governs timber harvesting practices on private land, demonstrates that government and landowners can work together and complete a project that benefits both the public and business interests; key public environmental values are being protected with no additional restrictions to land use; and private property rights are being respected.

TimberWest will continue to play a key role on the team of landowners working with government on the regulations and rules in support of this Act.

A renewed, competitive local sawmilling industry in BC

We are also committed to working with the BC government as it implements its long-awaited policy reforms governing the management of BC's Crown forest lands. The province is moving to a regime where market forces will be brought to bear on stumpage values, log prices, timber harvesting costs, and ultimately who owns how much tenure.

In terms of implementation efforts, progress was realized in 2003 with the abolition of appurtenancy and cut control requirements. The new tenure transfer provisions were also fully operative by year-end, and the introduction of the new market-based stumpage system was announced in early January 2004. We look forward to seeing the remaining elements of the change program implemented, including the revisions to Bill 13 contractor regulations and the tenure takeback program, so full market forces are in place.

TimberWest is also committed to working with the IWA to modernize our labour agreement and lower costs. We support the legislation passed by the provincial government in December to end the strike in the coastal forest industry and we are encouraged by the appointment of Donald Munroe as mediation-arbitration commissioner and by his terms of reference. The commissioner must consider the need for terms and conditions of employment that are consistent with the economic viability and competitiveness of the coastal forest industry in both the short and long term, the importance of good labour-management relations, and the interests of the employees and trade unions. I believe it is fair to say that both sides in this dispute recognized the need for some assistance in coming to a satisfactory resolution to this dispute.

We are hopeful that the market reforms introduced by the province, combined with a modernized labour agreement in 2004, will go a long way to rejuvenating the public land segment of the BC coastal forest industry. Re-establishing a vibrant and competitive sawmill industry on the coast, which is capable of paying international prices for its logs, will be beneficial to TimberWest's private land business.

LOOKING FORWARD

TimberWest faces a challenging environment in 2004, but there is reason for optimism, as we expect to finish the year with a reduced cost structure. Our challenges come to us in the form of a strong Canadian dollar, near-flat log prices, and continuing uncertainty on the softwood lumber file. Our optimism is driven by the prospect of a new labour contract by May that, combined with diligent cost reduction strategies, should result in additional cost savings. We also foresee a stronger domestic log market as local sawmills reduce costs and increase lumber shipments to the Japanese market.

We will continue to focus on our Operations Excellence strategy and moving closer to our core business model through the sale of TFL 46. In a stable-to-improving log price environment, these are strategies that will increase cash flow.

I thank all TimberWest employees and contractors for working so hard during such difficult conditions and for remaining focused on Operations Excellence. I also thank our customers and unitholders.

Paul J. McElligott, *President and CEO*
January 21, 2004

Stapled Units

Stapled Units are a unique form of security that combines the attributes of common shares, preferred shares and debt in a single security. TimberWest Forest Corp. Stapled Units consist of one common share, 100 preferred shares and approximately $8.98 face amount of Series A Subordinate Notes. These are "stapled" together as a single unit trading on the Toronto Stock Exchange under the symbol TWF.UN. Holders of TimberWest Stapled Units receive annual interest income of approximately $1.08 per Stapled Unit on the Subordinate Note component. Cash in excess of this amount may be distributed as declared by the Company's Board of Directors.

From the Chairman

It was a difficult year for TimberWest in 2003, with over-supplied markets, a rising Canadian dollar, the ongoing softwood lumber dispute with the US, severely dry summer conditions and a strike by the IWA.

Given these external pressures, TimberWest did not generate sufficient cash to cover our distribution in 2003. The Company paid out $82.1 million in distributions to its unitholders in 2003, while generating $51.4 million in distributable cash from operations. The Company has a policy of maintaining an even distribution level in the event of annual operating fluctuations. In previous years we have generated more cash than required to fund distributions and, from inception to the end of 2003, the Company has generated distributable cash of $471.6 million and, including the January 2004 distribution of $20.5 million, it has paid out $484.3 million to unitholders. Without relying on the proceeds from the sale of the TFL 46 public lands, we expect cash from operations to more closely match distributions in 2004.

During the year, all employees have stayed the course with the Company's Operations Excellence strategy. By concentrating on factors we can control, employees have improved the Company in many ways during the two years since the strategy was launched. Creativity and innovation have allowed TimberWest again to cut costs. In particular, the private Timberland Operations have reduced their costs by $4.27 per m^3 or more than $10 million. As well, the silviculture team has assured a more profitable harvest in the future by developing a sophisticated monitoring and inventory program to analyze our existing forest, and by implementing a plan to improve the growth rate of new plantings.

I am pleased to report that TimberWest maintained our strong emphasis on working safely and on environmental stewardship in spite of the difficult economic year.

In a summer that was the driest in recorded history, TimberWest did not lose any of its tree farm estate to the widely publicized forest fires in British Columbia. Clearly our strategy of retaining TimberWest's Martin Mars water bombers to protect our land is the right one. In addition, both aircraft were extensively utilized under contract to the BC Forest Service in 2003.

The Board continues to operate on the basis of integrity and open communication with the entire senior management team. The Board has always worked to a high standard of governance and continues to monitor its policies and procedures to ensure it is leading the way with its governance model. In particular, under the chairmanship of Bill Brown, the Audit Committee continuously reviews financial policies, controls and practices of the organization.

During the year, the Board formed a Pension Committee to oversee the activities of the TimberWest Retirement Plan Committees with respect to funding and investment policy, administration and legislative compliance, and the appointment of actuaries, fund managers and advisors. Given the importance of this function, which was previously performed by the Audit Committee, the Board felt it prudent to establish a separate committee to govern pension matters.

The Board is confident that we comply with all governance standards as they currently exist, including our Code of Business Conduct and Ethics and our Code of Ethics for Senior Executives and Financial Officers, both of which will be published in our information circular and posted on our web site. We will continue to comply with new governance standards as they are implemented.

As CEO Paul McElligott points out in his letter, the Company will maintain its focus on Operations Excellence. The Board is confident that TimberWest will continue to be one of the forest industry's most respected companies.

V. E. Daughney

V. Edward Daughney, *Chairman of the Board*
January 21, 2004

▲ Left to right:

Chairman
Edward Daughney

Vice-President
of Timberland
Operations
John Mann

Vice-President of
Finance and CFO
Bev Park

Director
Anthony Petrina

Vice-President of
Human Resources
and Information
Technology
Mark Stock

Our key policy issues

SOFTWOOD LUMBER DISPUTE

In May 2002, the US Department of Commerce (DOC) imposed 18.8% countervail duties as well as company-specific anti-dumping duties on Canadian softwood lumber exported to the United States.

In 2003, US and Canadian governments participated in a series of meetings to try to reach a long-term resolution of the trade dispute based on changed circumstances. The DOC published its official policy bulletin outlining changes individual provinces would need to implement to achieve such a ruling. Once the framework for a long-term solution to the dispute was established, the two countries began discussing the possibility of an interim agreement.

In December, the US government presented a proposal that would cap Canadian lumber imports into the US at 31% market share and establish a quota system to allocate shipments across Canadian industry. Duties collected over the past few years would be shared between the US and Canada 49%-51%, respectively. In January 2004, two World Trade Organization (WTO) rulings were released. First, the WTO affirmed the DOC's finding that Canadian lumber is heavily dumped in the US. Second, the WTO Appellate Body confirmed that the provinces' below-value timber sales are a subsidy and that the subsidy can be measured through comparisons to US timber prices. The ruling on injury is yet to be made; however, even if this were made in Canada's favour, the US would file an appeal.

TimberWest supports a negotiated settlement. This would allow BC to focus on proceeding quickly with forest policy changes to ensure full market forces operate in BC, so logs are sold to domestic mills for international prices rather than at subsidy prices.

Further, TimberWest believes that some quota must be made available to new entrants. During 2003, the Company invested over $9.5 million in new capital to modernize its Elk Falls Lumbermill and added a third shift with 30 new employees, believing it would have equitable access to the US market with a resolution to the softwood lumber dispute. This is a dimension mill originally configured for US production and, with the recent capital additions, it is very much a "new entrant" requiring quota.

NOTICE 102

The export of private land logs out of BC is restricted by the federal government's surplus test, Notice 102. This test requires that private forest owners offer their logs up for sale first in BC at domestic prices (which are typically lower than export prices), and only if there is no buyer in BC can a private forest landowner then sell logs outside of the country. This restriction applies only to BC landowners. Private forest landowners in all other provinces, and in the US, are free to sell their logs to any customer they choose.

The price premium earned by selling private land logs into the export market represents more than half of the distributable cash generated by the Company. The ability to export private land logs has also played a key role in keeping employees working while most Crown timber–dependent companies were severely curtailed over the past couple of years. Selling logs at higher international prices allows owners of private land to harvest stands that would otherwise be uneconomic. Harvesting this wood keeps loggers working and, because only a portion of wood within a stand is of export quality, the remainder is available to BC sawmills to maintain jobs.

REALITY:
Forcing private forest landowners to sell logs to domestic sawmills at prices lower than the international price unfairly transfers the value from the tree grower to the processors.

Forcing private forest landowners to sell logs to domestic sawmills at prices lower than the international price transfers the value from the tree grower to the processors, impairs the value of private timberlands in coastal BC and reduces pricing on Crown logs sold in coastal BC. It is thus extremely important for TimberWest to have this discriminatory restriction removed.

In March 2003, the assistant deputy minister to Pierre Pettigrew publicly stated the federal government would remove these restrictions as part of a trade deal with the US. The US policy bulletin contains language regarding constraints that limit competition, such as "barriers to inter-provincial or international trade in private sector logs that affect the market to be used as a reference point." Thus it is clear that removing private land log export restrictions would favourably affect BC's chances of getting a positive ruling on changed circumstances.

On the legal front, in 2001 TimberWest filed a statement of claim in the Federal Court of Canada challenging the validity of the private land log export restrictions that apply only to BC, seeking a declaration that the provisions are of no force and effect. In December 2003, this legal action proceeded to examinations for discovery. The actual trial date is expected to be set for 2005.

BC POLICY REFORMS

In 2003, the BC government passed legislation to create a policy framework that eliminates the social engineering of the past and moves to market forces. Changes include the elimination of appurtenancy, cut control, 5% tenure takebacks on a change of control and the province's veto on a transfer of tenure or mill closure; making tenure divisible; a 20% takeback of Crown tenure to secure fibre for First Nations groups and for the auctions required for a market-based stumpage system; and a transitional stumpage system.

TimberWest is paying close attention to these changes to ensure the Company responds to maximize value for unitholders. For example, once the 5% tenure takeback was eliminated, the Company put TFL 46 up for sale.

While the government has clearly moved in the right direction by injecting market forces into the industry, it is TimberWest's view that these reforms alone are not going to ensure the future competitiveness of the industry or ensure that the province and investors realize the full economic potential of BC's forests. Perhaps these reforms are all the change the industry can handle at this time, but sometime soon the province should pilot test different tenure arrangements, like a two-rotation lease, which would bestow ownership-like rights on commercial timberlands. Evidence from other jurisdictions worldwide demonstrates all stakeholders would benefit from such a model.

FOCUS

Goals, strategies & results

- SAFETY
- COST REDUCTION
- MARKET EXPANSION
- STEWARDSHIP
- ENHANCING FOREST VALUES

It has been two full years since we launched Operations Excellence, and we are confident this has been the right strategy for us during these difficult times.

CONTEXT FOR A SUSTAINABLE STRATEGY

In 2001, TimberWest's senior management team and key operating personnel devoted considerable time and effort to the development of a long-term strategic plan: **Growing greatest value through Operations Excellence.**

TimberWest launched the strategy in early 2002.

At that time, it was clear that the coastal sawmilling and public timberlands industry was not viable in its current form, and would continue to restructure and consolidate. In terms of markets, 2001 witnessed eroding log prices in all regions, especially in the second half of the year, with oversupply exacerbating the situation. Pricing has continued to deteriorate since that time.

The Canada-US Softwood Lumber Agreement expired in 2001, only to be followed by the introduction of large countervail and anti-dumping charges on Canadian lumber shipments to the US. The softwood lumber trade dispute remained unresolved in 2003.

TimberWest's strong performance from 1998 to 2002 was attributable primarily to our successful market diversification strategy and the resulting increase in log exports to Japan, the US West Coast and emerging Asian markets.

Our ability to export logs also allowed us to keep most of our employees working, when all other coastal forest companies were taking extended downtime.

In our 2001 Annual Report, we pointed out that while gains made in log exports had been excellent, gains of a similar order of magnitude were not possible going forward. In addition, as we move increasingly into second-growth stands, the trees we harvest are smaller and our future end-use sorts will be different from our present sorts.

While the lower value of future end-use sorts will be partially offset by the reduced costs of highly mechanized second-growth harvesting, a new focus on operating performance improvements and quality will be important.

It was clear that our priority must be to improve performance in all of our businesses — private lands, public lands and our lumbermill — and that means cost reductions, improved productivity, and growing more trees faster on our private lands.

It has been two full years since we launched Operations Excellence, and we are confident this has been the right strategy for us during these difficult times.

We have made progress during 2003 on each of our five Operations Excellence goals — safety, cost reduction, market expansion, stewardship and enhancing the value of timberlands.

During the past two years, we have greatly improved our safety performance, cut costs by $20.6 million in Timberland Operations, made inroads into emerging Asian markets, operated in a sustainable fashion with a continued strong emphasis on environmental stewardship, and increased our high-value silvicultural treatments in order to grow more trees faster.

Our specific accomplishments and targets for 2004 are outlined in the following five pages.

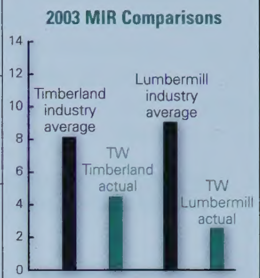
FOCUS

Safety

Our goal for 2003 was to achieve the best safety record in coastal BC for both logging and sawmilling.

		TARGET MIR*	ACTUAL MIR	TARGET SR**	ACTUAL SR
2003 PERFORMANCE:	Timberland Operations:	4.30	4.48	119	87
	Elk Falls Lumbermill:	4.00	2.56	N/A	N/A

		TARGET MIR	TARGET SR	% REDUCTION OF SR
2004 TARGETS:	Timberland Operations:	2.55	50	43
	Elk Falls Lumbermill:	2.55	50	N/A



***Medical Incident Rate (MIR)** is the number of recordable cases per 100 full-time equivalent employees per year. It is calculated by multiplying the number of cases by 200,000 and then dividing by the exposure hours worked by all employees.

****Severity Rating (SR)** is the number of days lost due to current year medical claims per 100 full-time equivalent employees per year. It is calculated by multiplying the number of days missed by 200,000 and then dividing by the exposure hours worked by all employees.

The number 200,000 is equivalent to 100 employees working 40 hours per week for 50 weeks.

PERFORMANCE OVERVIEW

Although Timberland Operations' MIR of 4.48 narrowly missed the target of 4.3, it showed a significant improvement of 18% over the previous year's safety performance. The SR of 87 is a 54% improvement from 2002's SR.

Elk Falls Lumbermill's MIR of 2.56, vs. the targeted 4.0, shows a 38% improvement over 2002, and is notable given the 21% increase in personnel and progression from two to three shifts due to expanded operations during the year. In 2003, the Planermill and Maintenance Departments achieved three years without a lost-time accident.

BEST PRACTICES

Early intervention: on-site therapy a boon to employees

After only one session with Certified Athletic Therapist Colleen Creighton, Rick Ryce could barely believe the difference.

"For several years I've been having problems with my hands. They would stiffen up and feel numb when I used them a lot, especially handling tools," says Ryce, Maintenance Welder at Honeymoon Bay Operation. "Sometimes I could work through it and they would limber up, but after the first therapy session I had instant relief."

Although not everyone who is treated by Creighton has received relief immediately, she and co-worker Heather Griffith of ErgoRisk Management Group Inc. have improved the comfort and physical well-being of many TimberWest employees. Through the Mobile Therapist Program, the two Certified Athletic Therapists travel to all of TimberWest's timberland and dryland sort operations on Vancouver Island to treat on-site clients suffering from work-related musculoskeletal injuries. Their mandate is early intervention, to help employees maintain or resume normal activities as quickly as possible after suffering discomfort or an injury.

After a brief pilot project, the program began full-time January 1, 2003. Three months later, it was expanded from one to two therapists to handle the increased demand due to positive outcomes.

"Musculoskeletal injuries often result from cumulative stress after a lifetime of physical labour. Such injuries are quite common in an aging workforce, which is exactly what we have. Our average employee in logging is 49 years old. Two years ago, about 60% of our lost-time incidents fell into this category, which is why we started this program," says John Mann, Vice-President of Timberland Operations.

Benefits became apparent almost immediately. People who suffered injuries that might have laid them up in the past were able to continue with their everyday activities after effective early intervention, including therapy, remedial exercises and/or ergonomic analysis of their work environments.

Creighton is not surprised at the results. "We bridge the gap between the workplace and rehabilitation, where in the past there was nothing," she says.

As for Ryce, not only is he able to work more efficiently, his overall quality of life has improved and he is often free from pain. "Whoever made this happen, I applaud their efforts," he says. "Things like this don't occur very often."

2003 ONGOING STRATEGIES & RESULTS

Develop measurable safety goals for which supervisors and managers are accountable. Require safety involvement of all employees and increase safety awareness

- Hired Health and Safety Program Manager in February 2003 to further develop programs and practices that increase involvement and safety awareness at all levels.
- Conducted Operational Safety Program audits for each operation.

Create consistent safety standards, procedures, practices and documentation

- Completed comprehensive Health and Safety Manual.
- Implemented site-specific Safety Operating Plans for every operation.
- Continued development of Safety Council to assist with standardizing safety procedures, practices and documentation.

Train employees in proper body mechanics, posture and movement, and early injury recognition. Practise early intervention

- Enhanced Mobile Therapist Program to assist employees with work-related musculoskeletal injuries, providing early intervention, which helps keep workers productive. The program was expanded from one to two therapists due to increasing demands and excellent performance-related outcomes for employees. (See story, right.)

Encourage knowledge transfer and pursue best practices

- Shared safety ideas with the union/industry SAFER Council to find and promote best practices throughout the industry.
- Conducted numerous specialized safety training sessions for management and employees. Elk Falls Lumbermill focused on extensive new hire safety training and contractor inductions.
- Vice-President of Timberland Operations served on Workers' Compensation Board (WCB) task force for safety improvement in the logging industry.

Work with WCB to optimize claims payments

- Implemented review of previous WCB claims that recovered $800,000 from incorrect claims adjudication.

TARGETS FOR 2004

More aggressive MIR and SR targets continue to be the focus for the future in Timberland Operations. Both targets are based on the philosophy that aggressive but achievable stretch targets are appropriate for moving quickly toward safety excellence. They also reflect the future reconfiguration of the Company with the pending sale of TFL 46. To improve safety performance in 2004, Timberland Operations will focus on:

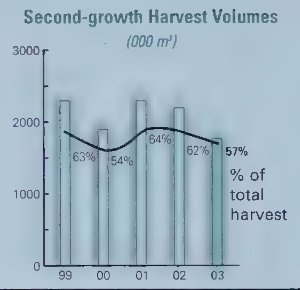
- Increased training of supervisors with a Loss Control Leadership self-study program.
- Ongoing changes to standardize Company health and safety documentation.
- Evaluation and standardization of managing contractor safety.

Elk Falls Lumbermill plans to increase training for safety representatives, particularly accident/incident investigation, and increase training/awareness in key areas, including mobile equipment and fall restraint.

Cost reduction

Our goal for 2003 was to become cost competitive on a global basis.

GOAL FOR 2003:	Reduce costs in Timberland Operations by $4.50 per m³.
ACTUAL FOR 2003:	Reduced costs in Timberland Operations by $0.99 per m³.



PERFORMANCE OVERVIEW

Timberland Operations cost-reduction initiatives generated $12 million in savings in 2003. However, significant deterioration of log markets, which led to increased inventories and public land logging curtailments, were followed by lost production due to extreme fire hazard and an IWA strike. These factors negatively affected indirect and fixed costs at some operations as well as regional, transportation and storage costs by a combined $8.9 million, accounting for the inability to meet 2003's target cost reduction. While private land operations were able to reduce their costs by $4.27 per m³, adverse effects from the above factors resulted in net cost reductions of $3.1 million or $0.99 per m³ on Timberland Operations overall.

Elk Falls Lumbermill decreased costs by $2 million in 2003, an 8% drop over similar costs in 2002. Successful implementation of a third shift and productivity gains achieved during the year have improved the mill's overall competitive position.

BEST PRACTICES

Fishbones and five why's: putting analytical thinking to work

For James Luxmoore, the "fishbone" made all the difference. For John Miller, it was the "five why's." Both men are referring to modelsfor root-cause analysis they learned through PERFOREX Management Training.

In 2002, Timberland Operations senior management determined that managers at all levels could benefit from analysis training in operational performance. In June 2003, PERFOREX, which works exclusively in the forest products industry, was secured to conduct training ranging from performance improvement to managing meetings effectively.

One of the most effective modules was root-cause analysis.

"The training was excellent," says Luxmoore, Engineer, Nanaimo Lakes Operation. "In our case, we felt gains could be made with our mechanical harvesting productivity. We were only getting about 15 hours of productivity out of each 16-hour double shift." The "fishbone" analysis, where each element or "bone" is analyzed as it leads into the "spine" of the problem, led Luxmoore and his team to one conclusion.

"We'd been 'hot-seating,' where one operator starts his shift as soon as the previous shift ends. But that was unrealistic — we weren't allowing time for refuelling or maintaining the equipment," he says. By introducing a one-hour gap between shifts for machine maintenance, the problem was solved.

In John Miller's case, they applied the "five why's" model to understand why trucks were sitting too long before being unloaded at dryland sorts. "The model makes you burrow deeper to find the root cause," says Miller, General Manager, South Island Operations.

The essential "why" of the problem with trucks waiting to be unloaded? They had been dispatched at staggered times from the landing sites, so a truck with a short haul might arrive at the same time as one with a long haul. The solution: stagger arrival times at the sort and work backwards from there, which resulted in more throughput and lower costs.

"PERFOREX gave the management team a common skill level, and focused us on key performance indicators and success factors," says Miller. "It's been a critical part of our action planning and follow-through, and definitely helped us achieve over $10 million in savings on our private lands last year."

2003 ONGOING STRATEGIES & RESULTS

Increase mechanized harvesting

- Increased mechanized falling from 42.5% of the total harvest done by Company crews in 2002 to 44.9% in 2003.
- Maintained high level of mechanized log processing (66.9% in 2003).
- Increased ground-based harvest systems from 37.3% of the total harvest done by Company crews in 2002 to 47.7% in 2003.

Improve operations planning and work methods with benchmarking and operational studies

- Used PricewaterhouseCoopers 2002 West Coast Log Cost Survey and Benchmarking Report to initiate benchmarking of suitable operators in Washington and Oregon.
- Implemented cost-reduction initiatives resulting from information gained through studies at the Forest Engineering Research Institute of Canada (FERIC) in the following areas:

> Sorting logs in the woods, which can then be scaled by weighing the loaded log truck.
> Increasing the volume transported in each yarding cycle by grapple yarding trees that have been bunched during mechanized falling.
> Using a grapple-equipped forwarder.

Identify and expand cost-saving initiatives

- Finalized bulk-purchasing agreements for a variety of supplies, including fuel and lubricants, explosives, bundle wire and culverts.
- Improved scaling and sorting costs by increasing the private land weigh-scale volume from 2% of total volume in 2002 to 10% in 2003. Costs were reduced by the ability to increase direct deliveries to end users.

Continue to reduce WCB premiums through improved safety performance

- Significantly improved 2003's Severity Rating, which showed a 54% decline from the previous year. This factor is key to reducing TimberWest's future WCB assessment rate.
- At Elk Falls Lumbermill, reduced WCB premiums by 20% off of base rates with improved safety performance.

At Elk Falls Lumbermill, continue to lower conversion costs

- Decreased unit conversion costs for aggregate savings of $2 million by:

> Adding a third shift (decreased conversion costs by 6%).
> Increasing planer efficiencies (decreased conversion costs by 2%).
> Improving lumber optimizing scanning technologies (reducing unit conversion costs by 1% through increased production).

TARGETS FOR 2004

Areas of focus for cost-reduction initiatives in 2004 in Timberland Operations will include the following:

- Optimize road construction standards by planning appropriately for the season and duration of use, and by managing risks with respect to environmental regulations.
- Expand cost-reduction opportunities through technological advances made by equipment manufacturers.
- Implement opportunities for cost improvement identified in the 2003 Equipment Fleet Maintenance Review.
- Optimize delivered log costs by increasing the volume of timber sorted in the woods.

At Elk Falls Lumbermill, improved safety performance in 2004 will realize a reduction in WCB premiums of 22% from base rates. The lumbermill will continue to strive to become a low-cost economic producer through emphasis on optimizing lumber processing, preventative maintenance and lumber recoveries.

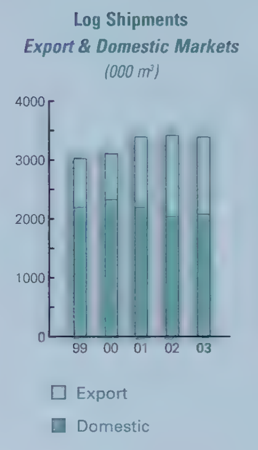
FOCUS

Market expansion

Our goal for 2003 was to diversify markets and maximize the return on all logs and lumber produced.

LOG SALES: BC continues to be TimberWest's primary market, accounting for 60% of the Company's log sales volume in 2003. During the year, the volume of log sales to the US dropped to 18%, while sales to Japan remained at 18%. Sales to emerging Asian markets doubled in 2003 over 2002.

LUMBER SALES: Key lumber markets were oversupplied in the first six months of 2003, leading TimberWest to divert some production into emerging markets. Even under adverse conditions, Elk Falls continued to find new market share as it moved product lines up the value chain, increasing sales for these products by 40% in 2003, representing about 13% of total production.



2003 ONGOING STRATEGIES & RESULTS

Log sales

Identify potential sales for emerging log markets

- Focused on emerging Asian markets in Korea, China and Taiwan. Increased sales by 100% to 71,000 m^3 in these markets, with the bulk of the growth occurring in Korea.

Select distribution channels and develop transportation logistics

- Developed additional distribution channels to Korea.
- Enhanced transportation efficiencies, which reduced cost of delivering logs to US customers.

Review strategic alliance or joint venture opportunities to improve margins

- Held preliminary discussions to establish a strategic alliance with J.S. Jones Timber Ltd., a recently constructed coastal sawmill capable of milling small-diameter hemlock sawlogs that were previously chipped for pulp.

Lumber sales

Expand sales of value-added products

- Developed products to serve North American railroads.
- Expanded kiln-dried product lines used in traditional Japanese homes.
- Currently developing products for application in engineered goods.

These developments contributed to further diversification of markets for the Elk Falls Lumbermill in 2003, as follows: Japan 44%, Canada 31%, USA 9%, Europe 9%, Australia 5% and China 2%.

TARGETS FOR 2004

TimberWest will investigate new opportunities for log sales in BC. Increased demand has been created by new capital investments in small log manufacturing, such as the new J.S. Jones Timber Ltd. sawmill, and in the veneer industry. The Company will also look at increasing the volume of logs purchased from external sources to facilitate programs at Elk Falls Lumbermill.

With kiln-drying capacity added in 2003, Elk Falls Lumbermill will continue to move product lines up the value chain and develop new markets for them, especially in Japan. Although lumber sales volumes to China and Asia are expected to drop in 2004, the Company will enhance the value of products bound for this region. Douglas fir markets in Japan, Europe, Australia and the US will be expanded. TW is also looking to develop new European markets for hemlock structural products. Success in 2004 will depend on diversification and adaptability.

BEST PRACTICES

Flexibility in bucking: making the most of old-growth fir

One of the most beautiful and valued elements a builder in Japan can add to a traditional *zairai* (post-and-beam) house is a long solid beam of Douglas fir with straight grain, free from knots.

TimberWest has long enjoyed a reputation for supplying its customers in Japan with old-growth logs suitable for the manufacture of such beams. However, with the declining quality of the old-growth timber profile, it became apparent that modifications were needed to maintain margins and market share.

"The change in the forest profile had moved us from an old-growth tree producing two logs suitable for Japan, to producing only one," says Roger Stewart, Log Scaling and Quality Superintendent. "The trees aren't as big any more, so our bucking program was limiting the log lengths we could cut."

For instance, a previously acceptable log length had been 10.4 metres, so if only 9.4 metres remained after bucking a log, the rest of the tree would be unacceptable. To compound the situation, customers in Japan prefer longer lengths.

"We consulted with our Japanese customers, who indicated that they wanted us to do what we could to improve the average length of old-growth Douglas fir logs," says John Mitchell, Manager, Operations Analysis and Harvest Support. "Longer lengths give them higher-value combinations."

Roger Stewart worked with Log Trader Steve Gillett and log manufacturing specialist Stewart Wheatley to come up with a revised set of bucking lengths that more than doubled the number of Douglas fir log lengths acceptable for beams, from four to nine.

The result? A 4% increase in the average log length of exported old-growth Douglas fir in 2003, a real positive especially considering the declining forest profile. (A one-foot increase in log length for these logs results in an increase in value of US$15 per thousand board feet.)

Customer response has been equally good. "Positive reactions from our customers in Japan have made it clear that the efforts of TimberWest in 2003 to modify our log bucking specifications to increase log length have, without a doubt, resulted in higher margins for them," notes Gillett.

"As well, increasing the average length of our old-growth fir has allowed TimberWest to expand our market share and increase margins."

FOCUS

Stewardship

Our goal for 2003 was to foster the Company's social licence to operate.

2003: In 2003, TimberWest continued its commitment to fostering sustainable forest management, maintaining water quality for domestic use and fishery values, mitigating environmental risk, and protecting key public environmental values and private timberland assets.

2003 ONGOING STRATEGIES & RESULTS

Maintain or enhance certification under Sustainable Forestry Initiative (SFI®) and ISO 14001

- Obtained ISO 14001 certification for the new North Island Dryland Sort. All of TimberWest's operations' and facilities' environmental management systems are certified under ISO 14001. The Company's private timberlands are also certified under SFI.
- Completed Land Use Management Plan, including analysis of long-term harvest levels, to consolidate policies and procedures used in sustainable forest management. KPMG Performance Registrar Inc. audited this plan to verify conformance with the SFI standard.

Continually improve environmental performance

- Completed an independent environmental policy review by a biologist and a water/soils specialist, including confirmation that adaptations to the Company's variable retention procedures improved forest productivity and employee safety while protecting key environmental values.

Maintain high standards of loss control

- Successfully protected assets through effective fire management systems during one of the highest fire-hazard seasons in history.
- Recorded top year for Flying Tankers Inc. working on fires throughout BC. Martin Mars water bombers revenue-generating hours from contract work increased 309% from 2002.

Maintain excellence in watershed management

- Reviewed proposed harvest plans within 100 watersheds and approved planned harvest activities on about 8,500 ha of private timberland within these watersheds.
- Completed three cycles of water quality sampling and analysis for domestic water use and fisheries values at 75 sites within sensitive watersheds on TW private lands.

Provide environmental management training and tools

- Trained foresters and engineers on ecological mapping and identification of plants requiring special management.
- Continued development of Terrestrial Ecosystem Mapping.

Work with partners to enhance the environment

- Continued partnership with the Pacific Salmon Foundation. Thirteen streamkeepers groups associated with TW's private lands received funding in 2003 to carry out fish habitat stewardship programs.
- Sold a 171 ha site for below market value to The Nature Trust of British Columbia to help protect high-priority fish habitat on the Englishman River.
- Continued support for the Marmot Recovery Foundation through a $130,000 contribution, for a total donation of $630,000 since 2000. In 2003, due to breeding work carried out by the recovery team, the total Vancouver Island marmot population increased to 108 from 99 marmots in 2002.
- Continued agreement with the Nature Conservancy of Canada to carry out ecological assessments including the mapping of areas around Sooke, Lake Cowichan and near Ladysmith.
- Partnered with Fisheries and Oceans Canada, Ducks Unlimited and NorskeCanada to enhance fish habitat in the Chemainus estuary.

Support organizations that improve quality of life in communities and regions where TimberWest operates

- Donated over $160,000 to more than 50 community service groups throughout Vancouver Island and in Vancouver. About 35% of donations went toward education, including the establishment of the Dr. Bob Willington Memorial Award at the University of British Columbia.

TARGETS FOR 2004

To further foster the Company's social licence to operate, in 2004 TimberWest will:

- Continue stewardship and water quality programs, and maintain certification.
- Finalize Terrestrial Ecosystem Mapping in 2004, which will result in TW's private lands having the most comprehensive land and forest classification system available.
- Continue inventories of red-listed species such as the Queen Charlotte goshawk and the marbled murrelet.

BEST PRACTICES

Making way for marmots

A Vancouver Island marmot named April will never know the chain of action her wandering ways set in motion last summer.

When a harvest block on the east slopes of Mount Washington — well away from known marmot habitat — was proposed for harvesting in early 2003, TW's Biologist Dave Lindsay and members of the Marmot Recovery Team, which is dedicated to restoring wild populations of this endangered species, gave the green light.

However, just as Oyster River Operations Planner Gary Lawson reported that harvesting was about to begin, researchers reported that April, a young female with an implanted radio transmitter, and a male friend had moved into the area.

"As soon as we found out the animals were in there, we didn't even start," says Lawson. Suddenly, 17,000 m^3 of timber were taken out of the 2003 harvest plan.

"We quickly had to move to an adjacent block earlier than planned to replace that volume. It's much more difficult to work because the road builders and fallers are in there at the same time. It takes about 15% more time and many extra precautions to ensure they're working safely," he adds.

As for April, researchers determined that she and her boyfriend were merely passing through. So the area is slated for harvest in 2004 with a modified plan that retains 6,000 m^3 of timber to accommodate April's possible return.

"It was quite remarkable," says Doug Janz, Fish and Wildlife Section Head, Ministry of Water, Land and Air Protection. "I have to applaud TimberWest for taking quick action once that information was known. Obviously their people on the ground are well aware of the implications of this type of issue."

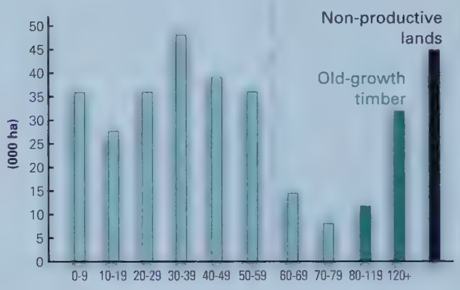
FOCUS

Enhancing forest values

Our goal for 2003 was to to increase the value of the operable private timberland base.

2003: Other than the fact that TimberWest's total shareholder return continues to outperform its peer group, it is difficult to measure the Company's achievements with respect to increasing the value of its operable private timberland base. However, a gap in value remains between the US Pacific Northwest land base and that in Canada. To close that gap, TW continues to undertake long-term strategies, including more intensive silvicultural practices and lower-cost harvesting.

Private Timberlands Age Class Distribution



2003 ONGOING STRATEGIES & RESULTS

Increase the growth rate of the forest

- Planted approximately 4.9 million seedlings in reforestation programs, 3.7 million on TW's private land and 1.2 million on Crown land. The long, dry summer in BC delayed by approximately three weeks the Company's summer planting programs to ensure that objectives for seedling survival and growth would not be compromised.
- Began implementing a plan to increase the growth rate of Douglas fir seedlings planted from the current 5% to nearly 11% by 2005. (The increase is over the growth rate of wild seedlings.) In the past, the Company's Mount Newton Seed Orchard was responsible for growing all of the seed TimberWest required. In 2003, by purchasing some of our seed from an outside source, TW staff were able to increase their focus on improving the growth rate of seedlings coming out of Mount Newton.
- Hired a full-time silviculture forester whose primary mandate is to increase timber production on TW's private land.
- Initiated the development of a comprehensive multi-year fertilization plan that will lead to enhanced timber yields. Due to various reasons, including the high cost of natural gas–based products such as fertilizer, TW did not conduct its fertilization program in 2003. The one-year interruption will not significantly affect forest growth.

Benchmark to ensure adoption of best practices

- Used information gained from benchmarking peer companies in the Pacific Northwest to develop a plan to increase vegetation management at time of planting. In combination with better tree breeding and effective fertilization, this is expected to reduce the time to harvest by 10%. Vegetation management is highly regulated and is used minimally, once in a 40- to 60-year rotation period on less than 1% of TW's land base in any one year.

Classify land base and improve access to information

- Cruised 15% of second-growth timber as part of the ongoing inventory plan.
- Produced TimberWest's first computer-generated 20-year harvest plan using new modelling software. This helps determine the most effective way to produce the highest yield per hectare.
- Upgraded forest information systems, with emphasis on silviculture record-keeping requirements to allow employees better access to information on the Company's land base.

TARGETS FOR 2004

TimberWest will continue to focus on growing more fibre in a way that generates more than the cost of capital and improving TW's growth-and-yield modelling capability. Strategies include the following:

- Implement a new silviculture strategy, to establish policies that maximize the value of TW's commercial timberland.
- Field check to determine expected increase in the long run sustainable yield. This entails gathering more detailed data on the time required for planted trees to reach 1.3 metres in height, and on how much timber is restricted by various constraints, such as riparian reserves.
- Integrate current late-rotation fertilization practices with TW's plan to fertilize some stands more than once during a rotation.
- Continue to collect inventory information and improve the accuracy of computer-generated 20-year logging plans.

BEST PRACTICES

Getting the best from the best of seedlings

They are called "plus" trees because they stand out in the forest. These are the super trees in nature — the ones that appear to grow faster, yield more and, with a little selection on the part of foresters, may also yield straighter, clearer grain.

Plus trees are only the first step of TimberWest's tree breeding program at its Mount Newton Seed Orchard near Victoria. The goal: apply the same old-fashioned techniques of grafting and cross-pollination scientists have used for centuries to continuously improve the performance of planted Douglas fir seedlings. Ultimately, these seedlings will generate a higher wood yield per hectare from TW's reforested sites.

Historically, TW's seed orchard program has provided average gains of 5% to 7% in seedling performance. In 2003, the Company hired full-time Silvicultural Forester Al Waters and initiated a plan to increase the performance of seedlings to nearly 11% by 2005 — a rate consistent with TW's best competitors in BC.

"Tree breeding is a no-brainer," says Hamish Kerr, Vice-President of Strategic Planning and Forest Policy. "It has a high effect on growth rates and yields a good rate of return on investment."

Key components of the program include better use of orchard seed and the purchase of seed from outside sources that will yield a 17% improvement in seedling performance.

"Purchasing outside seed raises the overall average performance of planted seedlings and takes the pressure off our own seed orchard to produce all requirements for the Company. Now Mount Newton can concentrate on developing our own seed with better performance," says Orchard Manager Tim Crowder.

Adds Waters, "If you plant trees that grow faster and produce 10 to 15% more timber per hectare, then your annual growth rate goes up, your harvest rate should go up, and so should your profit."

CONTENTS

MANAGEMENT'S DISCUSSION & ANALYSIS

Management's discussion and analysis provides an overview of TimberWest Forest Corp.'s business operations, as well as an examination of significant developments that have affected TimberWest's financial condition and results of operations for 2003 relative to 2002. Factors that could affect future operations are also discussed. These factors may be affected by known and unknown risks and uncertainties that may cause the actual future results of TimberWest to be materially different from those expressed or implied in this discussion.

This discussion and analysis should be read in conjunction with TimberWest's consolidated financial statements and the accompanying notes included in this annual report. TimberWest's consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles and are expressed in Canadian dollars. Certain comparative financial figures presented have been reclassified to conform to the presentation adopted in the current year.

This management's discussion and analysis has been prepared based on information available as at January 21, 2004, except where otherwise indicated. Additional information relating to TimberWest, including the Company's Annual Information Form and other statutory reports, can be found on the System for Electronic Document Analysis and Retrieval (SEDAR) at http://www.sedar.com.

ABOUT TIMBERWEST

TimberWest Forest Corp. (TimberWest or the Company) was incorporated on January 31, 1997. In June 1997, the Company acquired the coastal assets of TFL Forest Ltd. (formerly TimberWest Forest Limited), including 210,000 hectares of private timberlands, Crown timber tenures and lumbermill operations, all located on Vancouver Island, British Columbia. In December 1997, the Company acquired Pacific Forest Products Ltd.'s 124,000 hectares of private timberlands, also located on Vancouver Island.

With its timberland asset base, TimberWest is well positioned as the largest owner of private forest lands in Western Canada. The Company's 334,000 hectares of private lands are largely located on Vancouver Island and the majority of the land base supports the growth of Douglas fir, a premium tree species sought after for structural purposes. While ensuring that rigorous environmental and conservation practices for wildlife, water quality protection, biodiversity conservation and a wide range of other conservation goals are applied, the Company believes these lands can sustain a long-term harvest of 2.1 million to 2.5 million m^3 of logs per year.

TimberWest also holds five renewable long-term public tenures, including two Tree Farm Licences (TFLs) and three Forest Licences, which provide the Company with the right to harvest 1.3 million m^3 of logs per year from Crown lands. The management practices applied to these lands meet the stringent requirements of the Forest Practices Code of British Columbia Act and the Forest and Range Practices Act. In September 2003, TimberWest initiated an auction process for the sale of one of its TFLs, Tree Farm Licence 46 (TFL 46), and associated forest licences, and in early 2004, signed definitive agreements for the sale of these assets. TFL 46 and associated licences account for 0.5 million m^3 of the Company's allowable annual cut on Crown tenures.

TimberWest operates a lumbermill at Elk Falls on Vancouver Island that processes lower-value logs primarily sourced from public tenures. In addition, approximately 6,000 hectares of TimberWest's private forest lands have been identified as having greater value as real estate properties and are progressively being made available for higher uses.

Industry Overview

TimberWest operates exclusively in the solid wood segment of the forest industry, engaged primarily in the harvesting and sale of logs. The Company is unique in that most of its log production is sold on the open market, which provides considerable flexibility to meet market opportunities. The sale of logs accounts for approximately 80% of the Company's revenue.

The Company is well positioned to supply fibre to a diverse base of customers who participate in two of the larger wood-based housing markets in the world, the United States (US) and Japan. TimberWest's position in the supply chain as a net seller of logs provides the Company considerable flexibility in the harvesting and sale of its timber resources.

TimberWest's Vision & Strategy

TimberWest is a market-driven company with a vision of "Growing greatest value through Operations Excellence."

The Company's vision was developed as a result of extensive analyses undertaken in 2001, which included an examination of the competitive dynamics of the forest industry in which TimberWest operates; an assessment of the Company's strengths, weaknesses, opportunities and threats in this industry context; and a determination of the Company's core competencies.

The results of these analyses were summarized in the form of the five-year strategic plan, updated in 2003, under which TimberWest presently operates. A key conclusion drawn from these analyses was that TimberWest's first priority is to enhance the performance of its existing business units under a strategy focused on "Operations Excellence." Key tenets of Operations Excellence include operating in a safe and sustainable fashion, a strong emphasis on environmental stewardship, and improvements in financial performance through cost reductions, market expansion and strategic silvicultural investments.

While all of the Company's operations are integral to the success of each other, strategic objectives have been identified for each area and are described below.

TimberWest's Business

Private timberlands

Private timberlands refer to the portion of timberland assets that TimberWest owns in fee simple. Private land ownership has been an advantage as the harvesting flexibility has enabled the Company to quickly respond to changing market conditions. Wood harvested from private land is in most cases exportable, albeit with some restrictions, and this has resulted in much higher average sales realizations than those achieved in the domestic market. In addition, these lands have lower operating and regulatory costs than public lands and have a more valuable species mix, with the predominance of Douglas fir. As a result, these lands have generally allowed the Company to generate consistent returns in difficult markets in past years. These returns have been steady, predictable and relatively controllable for TimberWest.

In the near term, the Company will focus on Operations Excellence, which means expanding markets to achieve the highest return for its product, reducing costs throughout the business and investing in its existing business, including an increase in high-value silviculture treatments, with a view to increasing the Company's long run sustainable yield. TimberWest's primary business strategy continues to be the pursuit of Operations Excellence with its existing basket of assets. As the Company is successful in achieving sustainable reductions in unit costs, it will explore other ways to complement the asset base to increase value.

Public lands

TimberWest's Crown tenures represent approximately 38% of the total company harvest. These operations have not had consistent profitability since the inception of the Company. The major issue is not only the variability in historic performance but also the uncertainty surrounding future performance in light of both market and regulatory change. Tenure reform, along with ongoing restructuring in the coastal industry, brings uncertainty but also the opportunity that comes with change.

In September 2003, TimberWest initiated an auction process for the sale of TFL 46 and associated forest licences, and in early 2004, signed definitive agreements for the sale of these assets. This sale is subject to several conditions but is expected to close during the first half of 2004. The sale of TFL 46 will reduce the annual public land harvest by 510,000 m^3, reducing harvests from public lands to approximately 29% of the total company harvest. Under the agreements for the sale of TFL 46 TimberWest will retain some rights to acquire fibre from the purchaser in order to meet obligations under certain fibre supply agreements.

TimberWest is committed to its strategy of Operations Excellence on its remaining public lands. The Company's short- to mid-term focus is on reducing operating costs within public land operations and working with other industry stakeholders to reduce other costs of public timberland operations.

Lumbermill operations

TimberWest has a single lumber manufacturing facility, the Elk Falls Lumbermill located at Campbell River, British Columbia. The Elk Falls facility includes a medium-diameter log lumbermill, an integrated chipping facility, a planermill and dry kilns. The lumbermill processes medium-diameter logs either harvested from TimberWest's logging operations or traded or purchased specifically for this operation. Currently operating at three shifts per day, this lumbermill has an annual production capacity of 166 million board feet of lumber and 330,000 m^3 of wood chips.

Integral to maximizing the value of the Company's timberland assets is access to conversion facilities that can pay global prices for fibre. The strategic objective for the Elk Falls Lumbermill is to continue to improve its competitiveness by enhancing its product mix and improving its productivity and cost competitiveness. Being the lowest-cost producer possible will allow the mill to compete with the highest bidders for fibre and thereby help maximize the value of the Company's timberland base.

Higher-use properties & other revenue streams

TimberWest has a portfolio of higher-use properties that comprise approximately 6,000 hectares at any one time. These properties are identified as TimberWest determines them to be surplus to its harvesting requirements. TimberWest's vast land holdings also have potential value to be realized from other uses, such as coal bed methane gas and mineral rights.

TimberWest is committed to exploring opportunities to create additional value from its existing land base, including participation in real estate activity and the development of other revenue streams where value may be added.

Key Performance Drivers

TimberWest operates in an international commodity market, and key to the Company's performance is the ability to be the lowest-cost producer possible. This is the key driver in delivering value to the Company's unitholder base. Hence, the crux of TimberWest's Operations Excellence strategy is to ensure all operations are producing at the lowest possible cost. As such, the Company has benchmarked all operating processes and has put in place productivity targets for labour and equipment that are designed to place all operations in the top quartile of industry performance in the shortest time frame possible.

Lowering costs, however, cannot come at the expense of product quality or margin, so earnings and cash flow measures are continually monitored to ensure the Company is improving its return-to-log.

Capability to Deliver Results

Financial capability

TimberWest is conservatively financed and has a low cost of capital. The Company has a debt-to-total-capitalization ratio of 22.6% and has considerable financial flexibility in distributing cash to its unitholder base and for investing in the Operations Excellence strategy where required. Within the past year, the Company accessed the Canadian debt market as well as the Canadian bank market for financing on favourable terms.

Non-financial capability

TimberWest has a highly skilled workforce — from its management team and its Board of Directors through to hourly employees and contract crews. During the past year, the Company's management team worked well together and is solidly behind TimberWest's strategic direction. The Company also has effective internal control and management information systems that ensure good decisions are being made and that relevant and timely information is being disclosed to the capital markets. TimberWest has invested in people, equipment, roads and inventory at appropriate levels to ensure that production can respond to changing market conditions.

HIGHLIGHTS & SIGNIFICANT TRANSACTIONS

Sale of Tree Farm Licence 46 (TFL 46)

As disclosed in note 19 to the accompanying consolidated financial statements, on January 21, 2004, subsequent to TimberWest's 2003 fiscal year end, the Company signed a definitive agreement for the sale of its southern Vancouver Island public land operations, referred to as TFL 46. The sale is subject to several conditions and is expected to close during the first half of 2004. Sale proceeds on this transaction are expected to exceed the carrying value of the assets being disposed of and will be included in distributable cash.

The decision to sell TFL 46 was announced late in the third quarter of 2003 and the sale was undertaken through an auction process with qualified bidders. TFL 46 represents part of the Company's public land logging business, includes timber rights to an annual allowable cut of 510,000 m^3 on 83,546 hectares of Crown land and has been operated by TimberWest as part of its Honeymoon Bay operation on southwest Vancouver Island.

The decision to offer TFL 46 for sale was based on a strategic review of the Company's portfolio of assets and a focus on maximizing returns to unitholders. TimberWest's core business is its private timberlands — for other companies, owning and operating a TFL is a core business strategy, therefore they may place a higher value on TFL 46. With recent policy changes around the sale of tenures and other forest policy reforms in British Columbia, TimberWest believed an opportunity existed to realize better value for unitholders from TFL 46 by selling it at this time.

Forestry Revitalization Plan

In March 2003, the government of British Columbia (the Crown) introduced its Forestry Revitalization Plan (the Plan), which has subsequently been implemented, in part, through the Forestry Revitalization Act, the Forest and Range Practices Act and amendments to the Forest Act and Forest Practices Code of British Columbia Act. The Plan provides for significant changes to Crown forest policy and to the existing allocation of Crown timber harvesting rights to licensees. The changes in the Plan include the relaxing of cut control requirements, the elimination of appurtenancy and timber processing requirements, more flexibility to consolidate and subdivide forest tenures, increased freedom to transfer forest tenures without restriction or penalty and a market-based stumpage system. As well, licensees, including the Company, have had their aggregate allowable annual cut attributable to Crown lands reduced by 20%, with the first 200,000 m^3 exempt from this reduction, as well as a 20% reduction in the area of Timber Licences held outside of a TFL. The Plan states that approximately half of this volume will be redistributed to provide opportunities for woodlots, community forests and First Nations and the other half will be made available for public auction. The Crown has acknowledged that licensees will be fairly compensated for the value of lost harvesting rights and for improvements on Crown land.

TimberWest has been advised by the Ministry of Forests that it will be subject to a 200,000 m^3 tenure takeback to be allocated such that 168,000 m^3 will be taken back from TFL 46 and 32,000 m^3 from Tree Farm Licence 47 (TFL 47). While the total allowable annual cut has been identified for takeback, licensees have been notified that the identification of areas comprising this volume will not be completed until late 2004. Therefore, the Company will continue to operate on these TFLs according to its existing operating plans for 2004. In addition, while provisions for compensation have been made by the provincial government, the specifics will not be communicated until the areas have been identified. This takeback is not expected to have a material effect on TimberWest. The takeback on TFL 46 will not affect the pending sale of this Crown tenure.

Public Debenture Offering

On September 26, 2003, the Company added on to its existing debenture issue by completing a public offering of $65.0 million aggregate principal amount of 7.0% unsecured senior debentures due October 1, 2007. The debentures were sold at a price of 101.28% of their principal amount, with net proceeds to the Company of $64.4 million. The Company used these proceeds to reduce indebtedness under its revolving credit facilities. The Company also received accrued interest on these debentures from April 1, 2003, of $2.2 million.

Retirement of Debentures

The Company retired $106.5 million aggregate principal amount of its 6.5% debentures when they matured on March 3, 2003, settling this obligation with funds drawn on credit facilities available at the time of this transaction

Revolving Credit Facilities

On March 3, 2003, the Company completed and received short-term financing from a Canadian bank in the amount of $40.0 million pursuant to an unsecured 364-day committed revolving facility due on March 1, 2004. Under this facility, funds are available to the Company in both Canadian and US dollars by way of adjusted prime rate–based loans, Canadian dollar bankers' acceptances and letters of credit or guarantee.

On May 28, 2003, the Company completed

and received additional short-term financing from a Canadian bank in the amount of $40.0 million pursuant to an unsecured 364-day committed revolving facility due on May 26, 2004. Under this facility, funds are available to the Company in both Canadian and US dollars by way of prime rate–based loans, LIBOR loans, Canadian dollar bankers' acceptances and letters of credit or guarantee.

On June 27, 2003, the Company completed a two-year extension to its $125.0 million unsecured revolving facility. This facility is now due on June 30, 2006, and continues to provide funding to the Company in both Canadian and US dollars by way of adjusted prime rate–based loans, bankers' acceptances, US rate–based loans, LIBOR loans and letters of credit or guarantee.

Accounting Policy Changes

Stock-based compensation & other stock-based payments

Effective January 1, 2003, the Company changed its policy of accounting for Stapled Unit option awards in accordance with the recommendations of the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3870 — *Stock-based Compensation and Other Stock-based Payments.* Section 3870 establishes standards for the recognition, measurement and disclosure of stock-based compensation and other stock-based payments made in exchange for goods and services provided by employees and non-employees. It applies to transactions in which common shares, stock options or other equity instruments are granted or liabilities incurred based on the price of common shares or other equity instruments.

In fiscal 2002, the Company adopted the recommendations of Section 3870 in effect at that time and elected to continue with its previously established policy that no compensation cost was recorded on the grant of Stapled Unit options to directors, officers or employees who are in active service or employment of the Company or of any of its subsidiaries, and complied with the requirement to provide additional disclosure of the effect of stock-based awards on net income and earnings per Stapled Unit on a pro forma basis.

During 2003, Section 3870 was amended to require recognition of expenses for all employee stock-based compensation transactions, including awards of Stapled Unit options, for fiscal years beginning on or after January 1, 2004. The Company made the decision to early-adopt the amendments to Section 3870 and effective January 1, 2003, has recognized a stock-based compensation expense using the fair value method for all employee stock-based compensation transactions, including awards of Stapled Unit options entered into on or after January 1, 2003. The Company has elected to adopt the recommendations of Section 3870 on a prospective basis and has not applied the fair value–based method of accounting to Stapled Unit options granted between January 1, 2002, and December 31, 2002.

Cash flow and other per share information

Effective June 30, 2003, the Company adopted the recommendations of the CICA Handbook Section 1540 — *Cash Flow Statements* and Section 3500 — *Earnings per Share.* Section 1540 and Section 3500 were amended during 2003, prohibiting the presentation of cash flow information on a per share basis in the financial statements, except for dividends or similar distributions in cash, paid or payable, to shareholders or unitholders.

In compliance with the amendments to Section 1540 and Section 3500, the Company will no longer be including separate statements of distributable cash as part of its consolidated financial statements. In addition, the Company will no longer be disclosing earnings information for the components of its equity. instrument, the Stapled Unit, in its consolidated financial statements other than earnings attributable to the common share component on a per common share basis. The statement of distributable cash and related earnings information are now included in management's discussion and analysis.

Future Accounting Standard Change

In 2001, the CICA Accounting Standards Board (AcSB) commenced a project to amend the amend the requirements in CICA Handbook Section 3860 — *Financial Instruments — Disclosure and Presentation* concerning the balance sheet presentation of financial instruments, or their components, as liabilities or equity. The project was undertaken to improve consistency with guidance issued by both the US Financial Accounting Standards Board and the International Accounting Standards Board. Standards issued by each of these agencies require obligations that may be settled at the issuer's discretion by the issuance of its own equity instruments be presented as liabilities and not as equity.

In June 2003, the AcSB issued an exposure draft proposing a revision to Section 3860 that would require obligations that may be settled at the issuer's option by a variable number of the issuer's own equity instruments to be presented as liabilities. In November 2003, the AcSB approved this revision to Section 3860 effective for all fiscal years beginning on or after November 1, 2004.

The revision to Section 3860 will have a considerable effect on the financial statement presentation of the Company's Stapled Units and the distributions paid thereon, despite the fact that the Company's financial condition and economic underpinnings remain unchanged. The calculation of distributable cash generated by the Company will not be affected by this revision.

The Company's Stapled Units are a unique equity instrument, consisting of one common share, 100 preferred shares and approximately $8.98 face amount of Series A Subordinate Notes. These components are "stapled" together as a single unit and trade together on the Toronto Stock Exchange as Stapled Units. Components cannot be transferred except with each other as part of a Stapled Unit. The Company has historically classified all components of the Stapled Unit as equity on its balance sheet as the Company's Subordinate Notes have a "Common and/or Preferred Shares Payment Election." This election provides the Company with the option to satisfy its obligation to pay any interest on the Subordinate Notes by delivering common and/or preferred shares and with the option to pay the principal amount of the outstanding Subordinate Notes by delivering common shares.

Given that the number of shares required to retire the Subordinate Note component is not fixed, the revision to Section 3860 requires that the Company reclassify the Series A Subordinate Note component of the Stapled Unit from equity to liabilities. Had the revision to Section 3860 been implemented by the Company for its 2003 fiscal year, the reclassification of the Subordinate Note component of the Stapled Units from equity to liabilities would have been $684.6 million.

Further, holders of the Company's Stapled Units are entitled to annual interest payments on the Subordinate Note component of approximately $1.08. For the same reason that the Subordinate Note component is currently classified as equity on the Company's consolidated financial statements, interest payments on Stapled Units are currently charged directly to retained earnings, on an after-tax basis, as a distribution similar to dividends on common shares.

The revision to Section 3860 will require distributions on Stapled Units to be reported, on a pre-tax basis, as an interest expense on the statement of operations. This revision also requires the tax benefit provided by the distributions to be reported as a component of the income tax provision on the statement of operations. Distributions on Stapled Units for fiscal 2003 were $82.1 million and the tax benefit recognized thereon was $17.4 million. Had the revision to Section 3860 been implemented by the Company for its 2003 fiscal year, a net charge to earnings of $64.7 million would have been required.

RESULTS OF OPERATIONS

The following table presents distributable cash generated by TimberWest for the year ended December 31, 2003, in comparison to distributable cash generated for the years ended December 31, 2002 through December 31, 1999:

(in millions of dollars except per Stapled Unit amounts) Consolidated Statements of Distributable Cash	2003	2002	2001	2000	1999 (restated)[1]
Net earnings	$ 24.8	$ 39.3	$ 44.6	$ 204.9	$ 20.7
Income tax benefit related to distributions	17.4	26.7	29.4	32.6	26.6
Earnings available for distribution[2]	42.2	66.0	74.0	237.5	47.3
Future income tax recovery	–	(0.2)	(15.2)	(170.8)	(8.9)
Write-down of property, plant and equipment and related costs	–	–	–	1.3	24.7
Earnings available for distribution before provision for future income taxes and write-down of property, plant and equipment and related costs	42.2	65.8	58.8	68.0	63.1
Add (deduct):					
Depreciation, depletion and amortization	11.2	15.2	17.0	17.1	18.7
Proceeds from sale of property, plant and equipment	11.4	19.4	12.4	11.3	9.7
Proceeds from sale of other assets	–	–	–	4.2	1.5
Gain on sale of property, plant and equipment	(3.7)	(3.9)	(2.5)	(2.0)	(2.7)
Additions to property, plant and equipment	(18.0)	(11.5)	(7.3)	(10.3)	(6.6)
Other non-cash items	8.3	5.1	5.1	0.9	(0.4)
	9.2	24.3	24.7	21.2	20.2
Distributable cash[2]	$ 51.4	$ 90.1	$ 83.5	$ 89.2	$ 83.3
Basic and diluted earnings available for distribution before provision for future income taxes and write-down of property, plant and equipment and related costs per weighted average Stapled Unit[2]	*$ 0.55*	*$ 0.88*	*$ 0.90*	*$ 1.02*	*$ 0.91*
Basic distributable cash per weighted average Stapled Unit[2]	*$ 0.67*	*$ 1.21*	*$ 1.29*	*$ 1.34*	*$ 1.20*
Diluted distributable cash per weighted average Stapled Unit[2]	*$ 0.67*	*$ 1.20*	*$ 1.29*	*$ 1.34*	*$ 1.20*
Cash distributions paid per Stapled Unit	*$ 1.08*	*$ 1.08*	*$ 1.08*	*$ 1.08*	*$ 1.08*
Basic weighted average number of Stapled Units outstanding (000's)	*76,234*	*74,686*	*64,984*	*66,590*	*69,608*
Diluted weighted average number of Stapled Units outstanding (000's)	*76,309*	*74,808*	*65,128*	*66,685*	*69,608*
Stapled Units outstanding at the end of the period (000's)	*76,246*	*76,193*	*64,691*	*64,825*	*69,608*

[1] Information presented for 1999 has been restated to reflect the retroactive effect of a mandatory change in methods of accounting for income taxes and employee future benefits for fiscal years beginning on or after January 1, 2000.

[2] Earnings available for distribution, distributable cash and basic and diluted earnings available for distribution and distributable cash per weighted average Stapled Unit are measures that do not have a standardized meaning prescribed by Canadian generally accepted accounting principles (GAAP) and may not be comparable to similar measures presented by other companies. Management believes that presentation of these measures will enhance an investor's understanding of the Company's operating performance.

Distributable Cash

TimberWest generated distributable cash of $51.4 million, or basic and diluted distributable cash of $0.67 per weighted average Stapled Unit, for the year ended December 31, 2003. This compares to distributable cash of $90.1 million, or basic distributable cash of $1.21 per weighted average Stapled Unit and diluted distributable cash of $1.20 per weighted average Stapled Unit, for the year ended December 31, 2002. Earnings available for distribution, before provision for future income taxes of nil, were $42.2 million, or $0.55 per basic and diluted weighted average Stapled Unit, in fiscal 2003. This compares to earnings available for distribution, before provision for a future income tax recovery of $0.2 million, of $65.8 million, or $0.88 per basic and diluted weighted average Stapled Unit, in 2002. The current year decline in distributable cash and earnings available for distribution before provision for future income taxes of $38.7 million and $23.6 million, respectively, reflects the effects of a 37% decrease in net earnings for 2003 compared to 2002. Oversupplied markets, a rising Canadian dollar, the ongoing softwood lumber dispute with the US, severely dry summer conditions and a strike by the Industrial, Wood & Allied Workers (IWA) late in the year all put downward pressure on earnings in 2003. Distributable cash generated in 2003 was also affected by higher capital expenditures and lower proceeds from the sale of property, plant and equipment compared to 2002.

Despite this multitude of adverse conditions, TimberWest distributed $82.1 million, or $1.08 per Stapled Unit, to unitholders in 2003, consistent with distributions made by the Company in 2002. The Company had to borrow from available credit facilities to satisfy some of this requirement in 2003. Since TimberWest's inception in July 1997 to the end of 2003, the Company generated distributable cash of $471.6 million while paying out $463.8 million to unitholders to the end of the calendar year. The Company also paid its January 15, 2004, distribution to unitholders of $20.5 million.

The following table presents the results of TimberWest's operations for the year ended December 31, 2003, in comparison to the results for the years ended December 31, 2002 through December 31, 1999:

(in millions of dollars except per common share amounts)	2003	2002	2001	2000	1999 (restated)[1]
Consolidated Statements of Earnings					
Net sales	$ 428.5	$ 464.9	$ 461.9	$ 487.0	$ 456.6
Operating costs and expenses:					
Cost of products sold	346.5	340.1	346.3	363.1	337.0
Depreciation, depletion and amortization	9.8	11.5	13.4	13.6	15.2
Selling, administrative and other	13.5	14.0	15.0	14.1	13.9
	369.8	365.6	374.7	390.8	366.1
Operating earnings	58.7	99.3	87.2	96.2	90.5
Interest expense	16.0	15.3	23.4	24.5	21.8
Amortization of debt issue costs	1.4	3.7	3.6	3.5	3.5
Other (income) expense	(1.8)	(0.9)	–	(0.6)	0.8
Loss on bond lock transaction	–	5.0	–	–	–
Restructuring charge	–	9.8	–	–	–
Write-down of capital assets and other related costs	–	–	–	1.3	24.7
Earnings before income taxes	43.1	66.4	60.2	67.5	39.7
Income tax expense (recovery)	18.3	27.1	15.6	(137.4)	19.0
Net earnings	$ 24.8	$ 39.3	$ 44.6	$ 204.9	$ 20.7
Basic earnings (loss) per common share	*$ (0.52)*	*$ (0.21)*	*$ 0.06*	*$ 2.49*	*$ (0.40)*
Diluted earnings (loss) per common share	*$ (0.52)*	*$ (0.21)*	*$ 0.06*	*$ 2.48*	*$ (0.40)*

[1] Information presented for 1999 has been restated to reflect the retroactive effect of a mandatory change in methods of accounting for income taxes and employee future benefits for fiscal years beginning on or after January 1, 2000.

Revenues

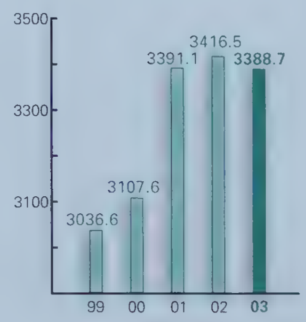
Net sales for the year ended December 31, 2003, were $428.5 million, down 8% from $464.9 million in sales reported for the year ended December 31, 2002.

Log sales for the year ended December 31, 2003, were $340.1 million, or 79% of total sales, compared to $378.2 million, or 81% of total sales, for 2002. The 10% decrease in overall log sales reflects the net effect of a 10% decrease in average log sales realizations and a 1% decrease in the volume of logs sold relative to 2002. Overall log sales realizations for 2003 averaged $100 per m³ compared to $111 per m³ for 2002, with realizations on domestic sales dropping 9% from the prior year to $86 per m³ and realizations on export sales dropping 8% from the prior year to $124 per m³. Log sales realizations were down primarily as a result of the rapid appreciation of the Canadian dollar against the US dollar during the year, and also due to weakness in end markets and the production of a weaker end-use sort mix in 2003.

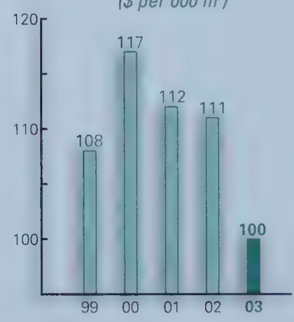
Log sales in 2003 reflect a strong first quarter where log sales volumes were 41% greater than the comparative quarter in 2002, with domestic market sales for the first quarter of 2003 more than double those for the comparative quarter in 2002. The favourable results of the first quarter of 2003 were offset by weaker log sales through the balance of the year, reflecting factors described previously, including a strengthening Canadian dollar relative to its US counterpart, the effects of global weakness in lumber markets, a weaker fibre profile, weather-related curtailments during the unusually hot, dry summer and labour-related work stoppages in the fourth quarter.

Domestic log sales volumes in 2003 of 2,082.6 thousand m³ were up 2% compared to 2002, while 2003 export sales volumes were down 5% compared to 2002, to 1,306.0 thousand m³. Volumes sold to US markets in 2003 were down 14% compared to 2002, while volumes sold to Asian markets increased 4% over 2002. US and Asian markets accounted for 47% and 53% of 2003 export volumes, respectively, compared to 52% and 48% in 2002. The 2003 sales mix by species was comprised of 53% fir, 29% hemlock and 10% cedar, compared to 57% fir, 23% hemlock and 11% cedar for 2002.

Log Shipments
(000 m³)



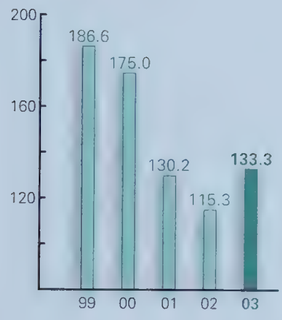
Average Log Sales Realizations
($ per 000 m³)



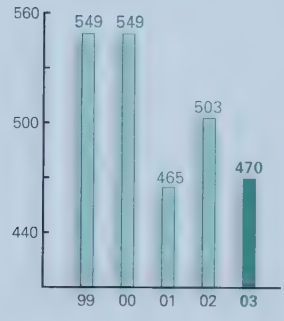
Lumber sales for the year ended December 31, 2003, were $62.6 million, or 15% of total sales. This compares to lumber sales of $58.0 million representing 12% of total sales for fiscal

2002. The 8% overall increase in lumber sales reflects a 16% increase in the volume of lumber sold, rising to 133.3 million board feet for 2003 from 115.3 million board feet for 2002, partially offset by a 7% decrease in average lumber sales realizations, falling to $470 per mfbm from $503 per mfbm for 2002. Adverse market and economic conditions prevailed throughout 2003 and have unfavourably affected operating results at the lumbermill for 2003 relative to 2002.

Lumber Shipments
(mmfbm)



Average Lumber Sales Realizations
($ per mfbm)



Capital and process improvements made at the Company's lumbermill in 2003 have resulted in an 11% increase in chip recoveries compared to those achieved in fiscal 2002. Wood chip sales for 2003 of $8.6 million were 13% greater than wood chip sales of $7.6 million in 2002, reflecting a 15% increase in chip volumes sold compared to 2002.

Real estate activities generated revenues of $8.6 million for the year ended December 31, 2003, compared to revenues of $16.5 million for 2002. Real estate sales reported for 2003 are considered to be typical, with 2002 sales being greater than normal due to the inclusion of proceeds of $11.5 million from the sale of the Company's Earle Creek property, a 2,400-hectare parcel of land located on the Sunshine Coast of British Columbia.

Operating Earnings

Operating earnings for the year ended December 31, 2003, were $58.7 million, or 14% of sales, compared to $99.3 million, or 21% of sales, for 2002. The 41% year-over-year decline in operating earnings is primarily attributable to the 8% decrease in overall net sales discussed previously and has been compounded by higher product costs in 2003.

On the Company's timberland operations, the operating margin for 2003 was 23%, down 6% from 29% of log sales for 2002, reflecting the effect of lower log sales realizations described above. Lower log sales realizations have been partially mitigated by cost reductions, a decrease in harvest volumes from higher-cost public lands and the use of lower-cost harvest systems. These factors contributed to a decrease in overall production costs to $73 per m^3, down from $76 per m^3 for 2002. The Company continued to make progress in achieving permanent cost reductions and increased productivity through strategic initiatives, with private timberlands delivering cost savings of $10.5 million, or $4.27 per m^3, in 2003. However, these costs savings were almost completely offset by the absorption of fixed costs on the public lands, resulting in an overall reduction in log production costs of $3.1 million, or $0.99 per m^3 against the Company's target of $4.50 per m^3. Cost savings in 2003 were the result of a wide range of initiatives, including direct shifting changes, increased harvest mechanization and system changes, improved rates and increased production through competitive bid work done by contractors, wage labour compliance changes, fleet management, bulk purchasing, facilities consolidation and overhead reductions. Logging cost of sales for 2003 was adversely affected by an increase in higher-cost log purchases over the prior year, with purchase volumes up 22% and the average purchase cost up 3%. Logging production volumes for 2003 were down 12% over 2002, to 3,132.6 thousand m^3, reflecting the net effect of increased harvests in the first quarter of 2003, offset by reduced harvests in the balance of the year due to market, weather and labour-related curtailments on timberland operations.

During 2003, the Company made a significant investment of $9.5 million at the Elk Falls Lumbermill toward capital improvement projects including three new lumber drying kilns and the replacement of the trimmer optimizer. The lumbermill was able to produce a higher-value mix of products in 2003, contributing to a 22% increase in the cost of products sold over the prior year, however, as noted previously, adverse market and economic conditions prevailed throughout 2003 and realizations on products were down across the board, resulting in an operating loss for the year. In addition, the lumbermill was forced to initiate several market-related shutdowns during the year, preventing the mill from fully leveraging improvements made. Given these conditions, despite the addition of a third shift to the lumbermill during the year, production at the lumbermill for 2003 was up only 3% over 2002.

Operating earnings were positively affected by real estate activity during the year ended December 31, 2003, contributing $1.6 million on property sales of $8.6 million, compared to $2.7 million on property sales of $16.5 million in 2002.

Earnings Before Interest, Taxes, Depreciation & Amortization

Earnings before interest, taxes, depreciation and amortization (EBITDA) for the year ended December 31, 2003, decreased $31.6 million to $70.3 million compared to $101.9 million for 2002. On a per weighted average Stapled Unit basis, EBITDA decreased to $0.92 for 2003, down from $1.36 in the prior year. For the year ended December 31, 2003, EBITDA as a percentage of sales decreased to 16%, down from 22% for the year ended December 31, 2002. These results were due to factors described previously.

The following table details the calculation of TimberWest's EBITDA for both fiscal 2003 and 2002:

(in millions of dollars)	2003	2002
Net earnings	$ 24.8	$ 39.3
Add:		
Interest expense	16.0	15.3
Loss on bond lock transaction	–	5.0
Income taxes	18.3	27.1
Depreciation, depletion and amortization	9.8	11.5
Amortization of debt issue costs	1.4	3.7
EBITDA[1]	$ 70.3	$ 101.9

[1] EBITDA does not have a standardized meaning prescribed by GAAP and may not be comparable to similar measures presented by other companies. Management believes that presentation of this measure will enhance an investor's understanding of the Company's operating performance.

Finance Charges

Interest expense for the year ended December 31, 2003, increased $0.7 million to $16.0 million compared to $15.3 million for the year ended December 31, 2002. This increase reflects the effect of higher debt outstanding during the year and an increase in the effective interest rate on credit facilities and debentures outstanding during the year.

The provision for amortization of debt issue costs of $1.4 million for the year ended December 31, 2003, was down from $3.7 million in 2002, primarily due to a higher provision in 2002 to record the amortization of fees associated with a non-revolving facility that settled in that year. The current provision reflects the deferral and amortization of $1.4 million in fees associated with the debenture public offering completed in September 2003, offset in part by the deferral and amortization of a $0.8 million premium received on this same public offering.

Financial results from 2002 include a one-time, pre-tax charge to earnings of $5.0 million representing the loss on a bond lock transaction entered into in anticipation of the 2002 public offering of $130.0 million aggregate principal amount of 7.0% debentures to protect against rising interest rates over the period of refinancing.

Restructuring Charge

Financial results from 2002 include a one-time, pre-tax charge to earnings of $9.8 million representing the expected costs of severance, early retirement programs and closure of facilities resulting from a restructuring undertaken during 2002 in an effort to streamline operations and increase efficiencies.

Income Taxes

Income tax expense for the year ended December 31, 2003, was $18.3 million compared to an expense of $27.1 million for the year ended December 31, 2002. The $18.3 million expense in 2003 includes current taxes of $0.9 million relating to large corporations tax and an income tax benefit of $17.4 million on interest on Series A Subordinate Notes held by unitholders, which has been offset by a credit directly to distributions. The $27.1 million expense in 2002 includes current taxes of $0.6 million relating to large corporations tax, an income tax benefit of $26.7 million on interest on Series A Subordinate Notes held by unitholders, which has been offset by a credit directly to distributions, and a net future income tax recovery of $0.2 million.

Net Earnings

Net earnings for the year ended December 31, 2003, were $24.8 million, down from $39.3 million for the year ended December 31, 2002. This decrease is due to factors described above, most notably a rising Canadian dollar, the effects of over-supplied markets, the ongoing softwood lumber dispute with the US, severely dry summer conditions and the strike by the IWA late in the year.

For the year ended December 31, 2003, TimberWest has reported a basic and diluted net loss per common share of $0.52, compared to basic and diluted net loss per common share of $0.21 for the year ended December 31, 2002. This year-over-year increase in loss per common share reflects the overall decrease in net earnings from that reported in the prior year, as well as the Company's unique equity instrument.

With TimberWest's Stapled Unit equity instrument, net earnings are first attributed to distributions on Series A Subordinate Notes. Earnings attributable to common shares are net earnings less net distributions on Series A Subordinate Notes held by unitholders (distributions announced during the year, net of the tax benefit thereon — see note 10 to the accompanying consolidated financial statements). In the current year, a $39.9 million loss is attributable to the common share component of the Company's Stapled Units, representing net earnings of $24.8 million less distributions announced during the year on Series A Subordinate Notes held by unitholders of $82.1 million, net of the $17.4 million tax benefit thereon. In 2002, a net loss of $15.8 million was attributable to the common share component of the Company's Stapled Units, representing net earnings of $39.3 million less distributions announced on Series A Subordinate Notes held by unitholders of $81.8 million, net of the $26.7 million tax benefit thereon.

Sensitivities

Markets for TimberWest's products are cyclical and affected by such factors as economic growth, interest rates, foreign exchange rates, construction activity and log and chip trading activities. The majority of the timber harvested from the Company's private timberland is sold at prices set by the Vancouver log market. Pricing in this market is affected by the prices of forest products that are produced from British Columbia coastal logs. TimberWest's earnings are subject to variation in log prices and therefore are subject to variations in forest product prices. In addition, TimberWest sells a substantial volume of product outside of Canada (51% of gross sales in 2003), mostly in US dollars. As such, the relative strength of the Canadian dollar versus its US counterpart has a considerable effect on sales and earnings.

The following table illustrates the sensitivity of TimberWest's operating earnings to changes in the average Canadian dollar selling price for its major products and in the value of the Canadian dollar relative to the US dollar:

(in millions of dollars)	Effect on operating earnings
Logs — $5 change per m^3	$ 16.9
Lumber — $10 change per mfbm	$ 1.3
Wood chips — $5 change per m^3	$ 1.2
Canadian dollar — $0.01 US change per Canadian dollar[1]	$ 2.9

[1] Estimate is based on US-dollar denominated sales for the year ending December 31, 2003, assuming all other variables remain constant.

QUARTERLY FINANCIAL HIGHLIGHTS

The following table presents selected unaudited quarterly financial information for each of the Company's last eight quarters. This data has been derived from unaudited interim consolidated financial statements that have been prepared on the same basis as the annual audited consolidated financial statements and, in the Company's opinion, include all normal recurring adjustments necessary for the fair presentation of such information. These unaudited quarterly highlights should be read in conjunction with the Company's audited annual consolidated financial statements.

Unaudited (in millions of dollars except per common share and per Stapled Unit and amounts)	2003					2002				
	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total
Net sales	$ 126.6	$ 109.3	$ 100.3	$ 92.3	$ 428.5	$ 88.9	$ 120.7	$ 130.4	$ 124.9	$ 464.9
Operating earnings	$ 30.5	$ 10.4	$ 12.0	$ 5.8	$ 58.7	$ 21.0	$ 19.3	$ 30.7	$ 28.3	$ 99.3
Net earnings (loss)	$ 17.7	$ 1.5	$ 6.3	$ (0.7)	$ 24.8	$ 7.7	$ 1.8	$ 12.9	$ 16.9	$ 39.3
Earnings available for distribution[1]	$ 25.4	$ 6.4	$ 9.6	$ 0.8	$ 42.2	$ 13.9	$ 4.0	$ 22.0	$ 26.1	$ 66.0
Earnings available for distribution before provision for future income taxes	$ 26.3	$ 6.4	$ 8.2	$ 1.3	$ 42.2	$ 14.9	$ 5.3	$ 22.0	$ 23.6	$ 65.8
Distributable cash[1]	$ 25.7	$ 4.7	$ 12.0	$ 9.0	$ 51.4	$ 21.2	$ 10.6	$ 34.1	$ 24.2	$ 90.1
Distributions paid	$ 20.5	$ 20.5	$ 20.6	$ 20.5	$ 82.1	$ 17.4	$ 20.4	$ 20.5	$ 20.6	$ 78.9
$ per common share										
Basic and diluted earnings (loss) per common share	*$ 0.06*	*$ (0.19)*	*$ (0.14)*	*$ (0.26)*	*$ (0.52)*	*$ (0.09)*	*$ (0.22)*	*$ 0.02*	*$ 0.07*	*$ (0.21)*
$ per Stapled Unit										
Earnings available for distribution[1]										
— basic	*$ 0.33*	*$ 0.08*	*$ 0.13*	*$ 0.01*	*$ 0.55*	*$ 0.20*	*$ 0.05*	*$ 0.29*	*$ 0.34*	*$ 0.88*
— diluted	*$ 0.33*	*$ 0.08*	*$ 0.13*	*$ 0.01*	*$ 0.55*	*$ 0.18*	*$ 0.05*	*$ 0.29*	*$ 0.34*	*$ 0.88*
Earnings available for distribution before provision for future income taxes										
— basic	*$ 0.35*	*$ 0.08*	*$ 0.11*	*$ 0.02*	*$ 0.55*	*$ 0.21*	*$ 0.07*	*$ 0.29*	*$ 0.31*	*$ 0.88*
— diluted	*$ 0.34*	*$ 0.08*	*$ 0.11*	*$ 0.02*	*$ 0.55*	*$ 0.20*	*$ 0.07*	*$ 0.29*	*$ 0.31*	*$ 0.88*
Distributable cash[1]										
— basic	*$ 0.34*	*$ 0.06*	*$ 0.15*	*$ 0.12*	*$ 0.67*	*$ 0.30*	*$ 0.14*	*$ 0.45*	*$ 0.32*	*$ 1.21*
— diluted	*$ 0.34*	*$ 0.06*	*$ 0.15*	*$ 0.12*	*$ 0.67*	*$ 0.28*	*$ 0.14*	*$ 0.45*	*$ 0.32*	*$ 1.20*
Distributions paid	*$ 0.27*	*$ 0.27*	*$ 0.27*	*$ 0.27*	*$ 1.08*	*$ 0.27*	*$ 0.27*	*$ 0.27*	*$ 0.27*	*$ 1.08*
Sales by product										
Logs	$ 103.8	$ 90.3	$ 76.2	$ 69.8	$ 340.1	$ 73.0	$ 102.9	$ 99.0	$ 103.3	$ 378.2
Lumber	16.6	14.7	14.8	16.5	62.6	12.7	13.0	14.1	18.2	58.0
Wood chips and other	3.6	3.8	5.9	3.9	17.2	2.5	3.1	3.3	3.3	12.2
Real estate	2.6	0.5	3.4	2.1	8.6	0.7	1.7	14.0	0.1	16.5
	$ 126.6	$ 109.3	$ 100.3	$ 92.3	$ 428.5	$ 88.9	$ 120.7	$ 130.4	$ 124.9	$ 464.9
Sales volume										
Logs *(thousand m³)*										
Domestic	566.3	511.6	470.3	534.5	2,082.7	267.2	615.8	507.5	650.8	2,041.3
Japan and other Asian markets	210.0	173.7	148.1	160.4	692.2	153.9	190.0	190.5	130.7	665.1
United States	143.1	230.8	168.3	71.6	613.8	228.7	219.7	132.0	129.7	710.1
	919.4	916.1	786.7	766.5	3,388.7	649.8	1,025.5	830.0	911.2	3,416.5
Lumber *(mmfbm)*	31.1	33.5	36.5	32.2	133.3	26.8	28.7	27.2	32.6	115.3
Production volume										
Logs *(thousand m³)*	892.8	852.1	669.4	718.3	3,132.6	707.5	1,023.9	859.4	969.1	3,559.9
Lumber *(mmfbm)*	35.5	39.5	16.5	33.2	124.7	26.0	30.9	31.3	33.3	121.5

[1] Earnings available for distribution, distributable cash and basic and diluted earnings available for distribution and distributable cash per Stapled Unit are measures that do not have a standardized meaning prescribed by GAAP and may not be comparable to similar measures presented by other companies. Management believes that presentation of these measures will enhance an investor's understanding of the Company's operating performance.

SUMMARY OF FINANCIAL POSITION

The following table presents summary information on TimberWest's financial position as at December 31, 2003, in comparison to balances as at December 31, 2002 through December 31, 1999:

(in millions of dollars)	2003	2002	2001	2000	1999 (restated)[1]
Assets					
Current assets	$ 70.1	$ 102.3	$ 91.6	$ 86.0	$ 96.7
Property, plant and equipment	1,356.5	1,355.6	1,369.1	1,384.3	1,396.8
Other assets	14.3	20.4	26.5	35.0	36.0
	$ 1,440.9	$ 1,478.3	$ 1,487.2	$ 1,505.3	$ 1,529.5
Liabilities and Unitholders' Equity					
Current liabilities	$ 110.0	$ 173.0	$ 262.2	$ 316.5	$ 82.7
Long-term financial liabilities	195.0	130.0	175.0	125.0	326.8
Other long-term liabilities	260.4	260.5	261.5	276.1	446.1
	565.4	563.5	698.7	717.6	855.6
Unitholders' equity	875.5	914.8	788.5	787.7	673.9
	$ 1,440.9	$ 1,478.3	$ 1,487.2	$ 1,505.3	$ 1,529.5

[1] Information presented for 1999 has been restated to reflect the retroactive effect of a mandatory change in methods of accounting for income taxes and employee future benefits for fiscal years beginning on or after January 1, 2000.

Current Assets

Current assets experienced a year-over-year decrease of $32.2 million to $70.1 million at December 31, 2003, down 31% from $102.3 million as at December 31, 2002. This decrease can be partially attributed to a $21.6 million decrease in inventories to $45.7 million at December 31, 2003, compared to $67.3 million at December 31, 2002. Log inventories of $41.1 million at the end of 2003 were $15.9 million, or 28% lower than log inventories of $57.0 million at the end of 2002, reflecting a 27% decrease in log volumes in inventory at year end as the result of lost production in November and December due to the labour-related work stoppages. Lumber inventories of $3.1 million at the end of 2003 were $5.4 million, or 64% lower than lumber inventories of $8.5 million at December 31, 2002, reflecting a 57% decrease in lumber volumes in inventory at year end, primarily due to a three week market-related curtailment in production at the mill in December 2003 and a greater proportion of higher-value Douglas fir product in 2002 year-end inventory. A $9.7 million decrease in trade accounts receivable to $15.4 million at December 31, 2003, down from $25.1 million at December 31, 2002, further contributed to the decrease in current assets, and can be attributed to the Company's efforts to manage this element of working capital and to lower log sales in the month of December due to lost production and the resultant decrease in product available for sale.

Property, Plant & Equipment

Property, plant and equipment of $1,356.5 million as at December 31, 2003, were $0.9 million greater than at December 31, 2002, reflecting the net effect of $18.0 million in additions to property, plant and equipment in 2003, offset by the current year provision for depreciation, depletion and amortization of $9.8 million and the sale of property, plant and equipment in the current year for proceeds of $11.4 million.

Other Assets

There was a net decrease of $6.1 million in other assets to $14.3 million as at December 31, 2003, compared to $20.4 million at the end of the prior year. Factors contributing to the net decrease in other assets include a decrease in prepaid pension costs of $2.9 million and a $1.4 million decrease in a receivable on the sale of other surplus assets.

Current Liabilities

Current liabilities at the end of 2003 were $110.0 million, down $63.0 million from $173.0 million as at December 31, 2002. This decrease can be attributed to several factors, most notably the retirement of $106.5 million aggregate principal amount of 6.5% debentures that were outstanding at the end of 2002 upon their maturity in the first quarter of 2003.

Current liabilities at December 31, 2003, include combined drawings of $60.0 million on two separate short-term credit facilities negotiated during the year. In the first quarter of 2003, the Company completed and received financing from a Canadian bank in the amount of $40.0 million pursuant to an unsecured 364-day committed revolving facility due March 1, 2004. In the second quarter of 2003, the Company completed and received additional financing from a Canadian bank in the amount of $40.0 million pursuant to an unsecured 364-day committed revolving facility due May 26, 2004.

Accounts payable and accrued liabilities decreased $16.5 million to $29.5 million at December 31, 2003, reflecting lower trade payables due to production curtailments in December 2003, lower stumpage fee accruals due to reduced harvests on Crown tenures during the fourth quarter and reduced compensation-related accruals under restructuring and incentive programs compared to balances as at December 31, 2002. The distribution payable at December 31, 2003, of $20.5 million is consistent with the distribution that was payable at December 31, 2002,

reflecting a consistent per unit distribution and no significant change in the number of Stapled Units outstanding during fiscal 2003.

Long-term Financial Liabilities

Long-term financial liabilities at the end of 2003 were $195.0 million, up from $130.0 million as at December 31, 2002, and at both year ends were comprised of the Company's 7.0% unsecured senior debentures due October 1, 2007. During the third quarter of 2003, the Company added on to its existing $130.0 million debenture issue by completing a public offering for an additional $65.0 million aggregate principal amount of the 7.0% unsecured senior debentures, increasing this obligation to $195.0 million at December 31, 2003.

As at December 31, 2003, the Company had additional long-term financing available under an unsecured revolving credit facility for $125.0 million. In the second quarter of 2003, the Company completed a two-year extension to this facility, which is now due on June 30, 2006. The Company had no borrowings on this facility at December 31, 2003, and December 31, 2002.

Other Long-term Liabilities

Other long-term liabilities as at December 31, 2003, included a silviculture liability of $4.6 million, a $25.3 million liability relating to non-pension post-retirement benefits and a future income tax liability of $230.5 million. These liabilities have not changed materially from the balances reported at December 31, 2002.

Unitholders' Equity

At December 31, 2003, unitholders' equity was $875.5 million, $39.3 million lower than as at December 31, 2002. This decrease is primarily due to a $39.9 million decrease in retained earnings during the year, which can be attributed to 2003 distributions on Series A Subordinate Notes held by unitholders of $82.1 million (net of the $17.4 million tax benefit thereon) exceeding 2003 net earnings of $24.8 million (see note 10 to the accompanying consolidated financial statements). In 2003, the stated value of Stapled Units increased by $0.5 million over the comparative year due to the issuance of Stapled Units on the exercise of Stapled Unit options during the year. As at March 1, 2004, the Company had 76,391,322 issued and outstanding Stapled Units, and 1,686,753 granted and outstanding Stapled Unit option awards.

Pursuant to a normal course issuer bid that expired on November 5, 2003, TimberWest was in a position to repurchase up to 3,809,201 of the Company's issued and outstanding Stapled Units through the facilities of the Toronto Stock Exchange. TimberWest did not repurchase any of its Stapled Units through this bid.

LIQUIDITY & CAPITAL RESOURCES

Operating

In 2003, operating activities provided TimberWest with $64.5 million compared to $74.2 million provided by operating activities in 2002. Net income, excluding non-cash items, generated cash of $51.3 million in 2003, down from $78.0 million in 2002. These decreases from 2002 were partially offset by the effect of changes in non-cash working capital items. The $13.2 million decrease in non-cash working capital during 2003 was due to the net effect of factors discussed previously under "Summary of Financial Position," including the Company's efforts to manage these elements of working capital and the effects of reduced production late in the fourth quarter contributing to a decrease in accounts receivable and inventories, offset in part by a decrease in accounts payable and accrued liabilities, to lower levels than typical of the fiscal year-end.

Financing

Cash used in financing activities was $63.7 million for the year ended December 31, 2003, compared to $83.9 million for the year ended December 31, 2002.

Financing activities in 2003 included $82.1 million in cash distributions paid to unitholders compared to $78.9 million in 2002. Though the distribution paid per Stapled Unit in 2003 remained unchanged at $1.08, an increase in the number of Stapled Units outstanding as a result of a public equity offering completed early in 2002 resulted in a $3.2 million increase in distributions paid in 2003.

During 2003, the Company issued 53,334 Stapled Units for net proceeds of $0.5 million on the exercise of Stapled Unit options during the year.

On September 26, 2003, the Company added on to its existing debenture issue by completing a public offering of $65.0 million aggregate principal amount of 7.0% unsecured senior debentures due October 1, 2007. The debentures were sold at a price of 101.28% of their principal amount, with net proceeds to the Company of $64.4 million after costs of $1.4 million. The Company used these proceeds to reduce indebtedness under its

revolving credit facilities. The Company also received accrued interest on these debentures from April 1, 2003, of $2.2 million, which was offset against subsequent interest payments on these debentures.

The Company retired $106.5 million aggregate principal amount of its 6.5% debentures when they matured on March 3, 2003, settling this obligation with funds drawn on credit facilities available at the time of this transaction.

During 2003, the Company completed and received short-term financings from two separate Canadian banks, each in the amount of $40.0 million pursuant to unsecured 364-day committed revolving facilities. One facility, due on March 1, 2004, makes funds available to the Company in both Canadian and US dollars by way of adjusted prime rate–based loans, Canadian dollar bankers' acceptances and letters of credit or guarantee. The second facility, due on May 26, 2004, makes funding available to the Company in both Canadian and US dollars by way of prime rate–based loans, LIBOR loans, Canadian dollar bankers' acceptances and letters of credit or guarantee. At December 31, 2003, the Company had net borrowings on these combined facilities of $60.0 million.

The Company also completed a two-year extension to its $125.0 million unsecured revolving facility during 2003. This facility is now due on June 30, 2006, and continues to provide funding to the Company in both Canadian and US dollars by way of adjusted prime rate–based loans, bankers' acceptances, US rate–based loans, LIBOR loans and letters of credit or guarantee. The Company had no borrowings on this facility at December 31, 2003.

Investing

Cash used in investing activities was $1.8 million for the year ended December 31, 2003, compared to $10.7 million provided by investing activities for the year ended December 31, 2002.

Proceeds from the sale of property, plant and equipment during fiscal 2003 were $11.4 million compared to $17.5 million for the prior year. These proceeds were generated primarily from the sale of real estate properties, representing $8.6 million and $16.5 million for 2003 and 2002, respectively. This year-over-year decrease can be attributed to the sale of TimberWest's Earle Creek property in 2002 for gross proceeds of $11.5 million. The sale of Earle Creek in 2002 was considered exceptional, given the unique nature of this property and its location on the Sunshine Coast of British Columbia. TimberWest's portfolio of higher-use properties has few comparable properties.

Additions to property, plant and equipment for the year ended December 31, 2003, were $18.0 million compared to $11.5 million for 2002. Major additions made during 2003 included $9.5 million toward improvement projects at the Elk Falls Lumbermill, including the purchase of three new lumber drying kilns and the replacement of the trimmer optimizer, $3.3 million to complete the North Island log sort and $2.5 million on road building activities for timberland operations. For 2004, the Company has committed to approximately $8.0 million in capital expenditures, including $4.1 million for timberland operations and $2.0 million for its Elk Falls Lumbermill.

A net decrease in other assets resulted in a net cash inflow of $4.8 million during 2003 compared to a net decrease in other assets of $4.7 million in 2002. The current year decrease in other assets was due in part to the Company collecting $1.4 million of a long-term receivable for a sale of other surplus assets.

Capital Resources

Excluding the credit facilities and the distribution payable to unitholders, net operating working capital was $40.6 million at December 31, 2003, compared to $56.3 million at December 31, 2002. TimberWest believes that its operating working capital is adequate to meet its operating requirements.

Total debt as at December 31, 2003, was $255.0 million compared to $236.5 million as at December 31, 2002. Total credit facilities available to the Company as at December 31, 2003, were $400.0 million, comprised of $40.0 million available under the 364-day revolving facility due March 1, 2004; $40.0 million available under the 364-day revolving facility due May 26, 2004; $125.0 million available under the revolving credit facility maturing on June 30, 2006; and $195.0 million of 7.0% debentures maturing on October 1, 2007.

TimberWest's consolidated debt-to-total-capitalization ratio as at December 31, 2003, was 22.6:77.4, slightly greater than 20.5:79.5 as at December 31, 2002.

In February 2004, the Company increased flexibility on all its bank credit facilities by obtaining an amendment to the Company's debt/EBITDA covenant. The amendment increases this test to 4.75:1 for the quarter ending March 31, 2004, from the previous level of 4.25:1.

COMMITMENTS NOT REFLECTED IN THE BALANCE SHEET

TimberWest does not have derivative financial instruments or any equity interests in unconsolidated entities or any other business arrangements related to the foregoing that would have a material effect on the results of operations or financial condition of the Company.

As disclosed in note 16 to the accompanying consolidated financial statements, in accordance with GAAP, TimberWest has commitments that are not reflected in the balance sheet of the Company. These commitments include operating leases for equipment and office premises and letters of credit that are routinely issued on behalf of insurance companies and other third parties in connection with outstanding performance contracts. As at December 31, 2003, commitments not reflected in the Company's balance sheet amounted to $40.6 million.

The following table provides a summary of all of the Company's future financial commitments as at December 31, 2003. This table details payments due in each of the next five years and thereafter, including commitments reflected on the Company's balance sheet and those that have not been reflected on the Company's balance sheet:

(in millions of dollars)	2004	2005	2006	2007	2008	2009+	Total
Reflected on the balance sheet							
Revolving credit facilities	$ 60.0	$ –	$ –	$ –	$ –	$ –	$ 60.0
Debentures	–	–	–	195.0	–	–	195.0
	60.0	–	–	195.0	–	–	255.0
Not reflected on the balance sheet							
Obligations under operating leases	11.8	7.5	3.4	1.4	0.6	0.6	25.3
Outstanding letters of credit	8.9	6.4	–	–	–	–	15.3
	20.7	13.9	3.4	1.4	0.6	0.6	40.6
	$ 80.7	$ 13.9	$ 3.4	$ 196.4	$ 0.6	$ 0.6	$ 295.6

UNIT TRANSACTIONS & INFORMATION

The following table sets forth quarterly closing prices and trading volumes of TimberWest's Stapled Unit and equivalent as traded on the Toronto Stock Exchange:

Trading of Stapled Units and Equivalent		Closing high	Closing low	Close	Volume
Trust Units/Stapled Units[1]:					
1997:	Third Quarter[2]	$ 16.00	$ 11.40	$ 15.00	8,046,941
	Fourth Quarter	$ 15.50	$ 9.90	$ 10.35	2,893,451
1998:	First Quarter	$ 11.60	$ 9.55	$ 10.50	9,786,692
	Second Quarter	$ 10.65	$ 8.20	$ 8.70	9,790,361
	Third Quarter[1]	$ 9.00	$ 7.60	$ 7.85	4,271,934
	Fourth Quarter	$ 10.00	$ 7.30	$ 8.95	8,486,269
1999:	First Quarter	$ 9.45	$ 8.50	$ 9.30	6,915,090
	Second Quarter	$ 11.75	$ 9.15	$ 11.50	5,498,035
	Third Quarter	$ 12.00	$ 10.55	$ 10.65	5,139,614
	Fourth Quarter	$ 10.85	$ 9.25	$ 9.50	8,047,352
2000:	First Quarter	$ 10.35	$ 8.80	$ 9.25	5,567,211
	Second Quarter	$ 11.30	$ 9.10	$ 10.40	4,094,791
	Third Quarter	$ 11.15	$ 9.85	$ 10.80	4,191,406
	Fourth Quarter	$ 11.00	$ 10.00	$ 10.85	2,231,067
2001:	First Quarter	$ 11.15	$ 10.60	$ 10.90	3,909,883
	Second Quarter	$ 12.50	$ 10.80	$ 12.20	2,430,870
	Third Quarter	$ 12.54	$ 11.65	$ 11.65	3,167,729
	Fourth Quarter	$ 13.25	$ 11.50	$ 13.00	4,834,500
2002:	First Quarter	$ 13.71	$ 12.75	$ 13.33	8,450,000
	Second Quarter	$ 14.00	$ 12.65	$ 13.96	5,766,665
	Third Quarter	$ 13.95	$ 12.50	$ 12.50	8,044,773
	Fourth Quarter	$ 12.81	$ 11.20	$ 12.00	5,614,688
2003:	First Quarter	$ 12.75	$ 11.75	$ 12.34	4,920,579
	Second Quarter	$ 12.90	$ 11.11	$ 11.30	13,497,139
	Third Quarter	$ 12.20	$ 11.09	$ 11.60	12,532,446
	Fourth Quarter	$ 12.79	$ 11.18	$ 12.70	10,859,497

[1] Trust Units of TimberWest Timber Trust ceased to be listed on the Toronto Stock Exchange (TSX) on October 9, 1998. Stapled Units of TimberWest Forest Corp. were listed on the TSX on October 6, 1998. Between October 2, 1998, and July 14, 1999, the Trust Units of the Trust were redeemable for Stapled Units of TimberWest on a one-for-one basis. On July 14, 1999, all remaining Trust Units except for 100 units held by TimberWest Forest Corp. were redeemed for Stapled Units.

[2] Trust Units were listed on the TSX on June 23, 1997.

CASH DISTRIBUTIONS

TimberWest's policy is to make quarterly distributions to its unitholders in the form of interest on the Series A Subordinate Notes held by unitholders. Quarterly distributions will be payable to the holders of Stapled Units of record on January 1, April 1, July 1 and October 1 in each year (Record Date) and are expected to be paid on the 15th day of the month of each Record Date. The Company may also make distributions as a return of capital upon the redemption of the preferred shares, or as dividends on the common shares or preferred shares. The amounts of such distributions are subject to TimberWest's overall financial condition.

Due to the nature of TimberWest's business, quarterly cash flows will fluctuate during the year for seasonal reasons. Cash flows will also fluctuate from year to year due to the cyclical nature of the business. One of the objectives of TimberWest's cash distribution policy is to make even distributions to unitholders. This means that cash distributions may vary from the actual cash generated during certain periods. Any difference will be added to or subtracted from either cash reserves or available credit facilities.

Total distributions paid to unitholders for the year ended December 31, 2003, were $82.1 million, or $1.08 per Stapled Unit outstanding at each Record Date, and were comprised entirely of interest earned on Series A Subordinate Notes. In 2003, TimberWest had to borrow from available credit facilities to satisfy some of this requirement. Since the Company's inception in July 1997 to the end of 2003, the Company has generated distributable cash of $471.6 million and, including the January 15, 2004, distribution of $20.5 million, the Company has distributed $484.3 million to unitholders.

The composition of distributions distributed to date on a per unit and equivalent basis were as follows:

Record date	Payment date	Interest income	Taxable dividends	Non-taxable[1]	Total distribution[2]
Trust Units:					
Sept. 30, 1997	Oct. 15, 1997	$ 0.259000	$ 0.066000	$ –	$ 0.325000
Dec. 31, 1997	Jan. 15, 1998	0.161000	–	0.089000	0.250000
		$ 0.420000	$ 0.066000	$ 0.089000	$ 0.575000
Mar. 31, 1998	Apr. 15, 1998	$ 0.266000	$ –	$ –	$ 0.266000
June 30, 1998	July 15, 1998	0.270000	–	–	0.270000
Sept. 30, 1998	Oct. 15, 1998	0.272000	–	–	0.272000
Dec. 31, 1998	Jan. 15, 1999	0.269457	–	–	0.269457
		$ 1.077457	$ –	$ –	$ 1.077457
Mar. 31, 1999	Apr. 15, 1999	$ 0.269364	$ –	$ –	$ 0.269364
June 30, 1999	July 15, 1999	0.269364	–	–	0.269364
		$ 0.538728	$ –	$ –	$ 0.538728
Stapled Units:					
Jan. 1, 1999	Jan. 15, 1999	$ 0.269457	$ –	$ –	$ 0.269457
Apr. 1, 1999	Apr. 15, 1999	0.269364	–	–	0.269364
July 1, 1999	July 15, 1999	0.269364	–	–	0.269364
Oct. 1, 1999	Oct. 15, 1999	0.269364	–	–	0.269364
		$ 1.077549	$ –	$ –	$ 1.077549
Jan. 1, 2000	Jan. 15, 2000	$ 0.269364	$ –	$ –	$ 0.269364
Apr. 1, 2000	Apr. 15, 2000	0.269364	–	–	0.269364
July 1, 2000	July 15, 2000	0.269364	–	–	0.269364
Oct. 1, 2000	Oct. 15, 2000	0.269364	–	–	0.269364
		$ 1.077456	$ –	$ –	$ 1.077456
Jan. 1, 2001	Jan. 15, 2001	$ 0.269364	$ –	$ –	$ 0.269364
Apr. 1, 2001	Apr. 15, 2001	0.269364	–	–	0.269364
July 1, 2001	July 15, 2001	0.269364	–	–	0.269364
Oct. 1, 2001	Oct. 15, 2001	0.269364	–	–	0.269364
		$ 1.077456	$ –	$ –	$ 1.077456
Jan. 1, 2002	Jan. 15, 2002	$ 0.269364	$ –	$ –	$ 0.269364
Apr. 1, 2002	Apr. 15, 2002	0.269364	–	–	0.269364
July 1, 2002	July 15, 2002	0.269364	–	–	0.269364
Oct. 1, 2002	Oct. 15, 2002	0.269364	–	–	0.269364
		$ 1.077456	$ –	$ –	$ 1.077456
Jan. 1, 2003	Jan. 15, 2003	$ 0.269364	$ –	$ –	$ 0.269364
Apr. 1, 2003	Apr. 15, 2003	0.269364	–	–	0.269364
July 1, 2003	July 15, 2003	0.269364	–	–	0.269364
Oct. 1, 2003	Oct. 15, 2003	0.269364	–	–	0.269364
		$ 1.077456	$ –	$ –	$ 1.077456
Jan. 1, 2004	Jan. 15, 2004	$ 0.269364	$ –	$ –	$ 0.269364

[1] Non-taxable represents a return of capital to unitholders, which reduces the cost base of the units.
[2] Excludes a distribution of $0.2 million made to holders of special deposit warrants on March 21, 1997.

CRITICAL ACCOUNTING POLICIES & ESTIMATES

TimberWest's accounting policies are described in note 2 to the accompanying consolidated financial statements. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

TimberWest considers the following policies to be most critical in understanding the judgments that are involved in preparing the Company's consolidated financial statements and the uncertainties that could affect the Company's results of operations, financial condition and cash flows.

Accounting for Private Timberlands

TimberWest accounts for its private timberland assets using the sustained yield method. Under the sustained yield method, depletion is taken on the capital cost of private timberlands if harvest levels exceed growth on a sustained basis. Yield analyses are conducted at least every five years on all private timberlands to determine if a depletion charge is required. The most recent yield analysis was completed in late 2003 and confirmed that the projected long-term harvest level from private timberlands is approximately 2.3 million m^3 per year and therefore no depletion charge is required for fiscal 2003.

The process of estimating sustained yield is complex, requiring significant decisions in the evaluation of timber stand volumes based on yield curves derived from data on timber species, timber stand age and growing site indexes gathered from a physical sampling of the timberland resource base. Although every reasonable effort is made to ensure that the sustained yield determination represents the most accurate assessment possible, subjective decisions and variances in sampling data from the actual timberland resource base make this determination generally less precise than other estimates used in the preparation of the consolidated financial statements. Changes in the determination of sustained yield may result in corresponding changes in the provision for depletion of the private timberland asset in periods subsequent to periodic yield analyses, and could result in impairment of the carrying value of capital assets.

Accounting for Series A Subordinate Notes

As TimberWest may elect to pay interest on the Series A Subordinate Notes held by unitholders in common or preferred shares of the Company, and may elect to pay the principal amount of the Series A Subordinate Notes held by unitholders in common shares of the Company, the $684.6 million principal amount of the Series A Subordinate Notes held by unitholders at December 31, 2003, has been classified as equity for accounting purposes, and interest thereon, on an after-tax basis, is charged directly to retained earnings as a distribution. The aggregate annual amount of interest payable on Series A Subordinate Notes held by unitholders at December 31, 2003, is $82.2 million.

In November 2003, the CICA AcSB approved a revision to CICA Handbook Section 3860 — *Financial Instruments — Disclosure and Presentation* that will require obligations that may be settled at the issuer's option by a variable number of the issuer's own equity instruments to be presented as liabilities, effective for all fiscal years beginning on or after November 1, 2004. TimberWest's Series A Subordinate Notes meet the criteria specified and effective the 2005 fiscal year must be reclassified to liabilities on the Company's balance sheet. Further, this revision will require that distributions on Stapled Units, currently charged directly to retained earnings, be reported, on a pre-tax basis, as an interest expense on the statement of operations, and that the tax benefit provided by the distributions be reported as a component of the income tax provision on the statement of operations. A detailed discussion of this issue is provided under "Highlights and Significant Transactions" in this management's discussion and analysis.

Accounting for Employee Future Benefits

TimberWest's pension and post-retirement benefit costs are developed from actuarial valuations. Inherent in these valuations are key assumptions, including the discount rate and expected long-term rate of return on pension plan assets. Material changes in TimberWest's pension and post-retirement benefit costs may occur in the future due to a change in these assumptions, a change in the number of plan participants or a change in the level of benefits provided.

RISK MANAGEMENT

TimberWest manages principal risks of its business through established systems and procedures in two main areas: business operations, including both forestry resources and facilities, and currency. The Company's principal risks can also be viewed in terms of controllable risks and non-controllable risks. Controllable risks relate primarily to the resources and assets of TimberWest and compliance with regulatory and ethical standards. Non-controllable risks result primarily from variations in product prices due to changes in market conditions, fluctuations in foreign currency exchange rates and regulatory, legislative and harvesting fee changes made by the provincial government of British Columbia.

Business Operations Risk

Revenues, net income and cash flow from TimberWest's operations are dependent on the Company's continued ability to harvest timber at adequate levels. The Company's ability to harvest timber from its timberlands in order to fund distributions to unitholders may be limited by weather conditions, timber growth cycles, market pricing, sustainable forestry standards and regulatory requirements. There can be no assurance that the Company will achieve harvest levels in the future necessary to maintain or increase revenues, net income and cash flows.

To minimize the potential for adverse effects arising from these risk factors, TimberWest has systems and procedures in place to monitor the utilization of resources and the protection of assets. Control mechanisms report on the efficiency and use of forestry, conversion and monetary resources. TimberWest believes that procedures in place to track and monitor changes, along with adequate insurance coverage, protect the Company's assets from undue business operations risk.

Forest resource risk

TimberWest's private timberlands and Crown timber tenures are subject to the risks associated with standing forests. Forest fires, insect infestation and disease pose the primary risks. The Company has endeavoured to minimize these risks through prevention and early detection. Fire protection is provided through ground-based suppression crews and an aerial attack capability provided primarily by TimberWest's Martin Mars water bombers. Over the last several decades, losses on the Company's private timberlands and Crown timber tenures due to fire, insect infestation and disease have been negligible. As is typical in the forest products industry, the Company does not maintain insurance coverage with respect to damage to its private timberlands. The Company does, however, maintain insurance for loss of logs due to fire and other occurrences following harvesting.

End-market risk

The results of TimberWest's operations are, and will continue to be, affected by the cyclical nature of the forest products industry. Prices and demand for logs and manufactured wood products have been, and in the future can be expected to be, subject to cyclical fluctuations. The demand for logs and wood products is primarily affected by the level of new residential construction activity and, to a lesser extent, repair and remodelling activity and other industrial uses, which are themselves subject to fluctuations due to changes in economic conditions, interest rates, population growth, weather conditions and other factors. Decreases in the level of residential construction activity generally reduce demand for logs and wood products, resulting in lower revenues, profits and cash flows.

The Company's business includes the sale of logs from its private timberlands for export, which is substantially dependent on market and economic conditions in both Japan and other parts of Asia, and the US West Coast region. Log export revenues may be affected by, among other things, log supply in competing regions, fluctuations in exchange rates, the availability of substitute products, the level of housing starts, changes in building practices and the effect of existing federal legislation that constrains log exports from private timberlands only in British Columbia. Historically, export grade logs have been sold at a premium over the prices that would have been received if the logs had been sold in the domestic market. British Columbia provincial legislation effectively constrains the export of logs originating from Crown timber tenures.

Regulatory risk

Legislation in British Columbia empowers provincial regulatory agencies to develop regulations, set policies and establish and maintain all aspects of sustainable forest management. The Forest Practices Code of British Columbia Act (Forest Practices Code), which was implemented on June 15, 1995, set standards of performance for forest practices on Crown timber tenures and private timberlands within TFLs, established planning procedures and set a range of activity-specific penalties for non-performance. Changes to the Forest Practices Code were announced on December 17, 2002, and in March 2003 the government of British Columbia introduced the Forestry Revitalization Plan, which provides for significant changes to Crown forest policy and the existing allocation of Crown timber tenures to licensees.

Initiatives implemented during 2003 focused on reducing bureaucracy, providing increased operating flexibility and reducing costs to Crown tenure

holders, while preserving environmental values; and included changes to the Forest Practices Code on stumpage, cut control, appurtenancy and tenure transfers. Further initiatives were introduced with the implementation of the Forest and Range Practices Act — a results-based forest practices code — early in 2004. The provisions of the Forest Practices Code is to be phased out and replaced by the Forest and Range Practices Act by December 31, 2005.

As part of the Forestry Revitalization Plan, the government also proclaimed legislation that authorizes a 20% takeback to the annual allowable cut for certain timber tenures in British Columbia after providing for an exempt amount, which in TimberWest's case is approximately 200,000 m^3. TimberWest has been advised by the Ministry of Forests that it will be subject to a 200,000-m^3 tenure takeback to be allocated such that 168,000 m^3 will be taken back from TFL 46 and 32,000 m^3 from TFL 47. While the total allowable annual cut has been identified for takeback, licensees have been notified that the identification of areas comprising this volume will not be completed until late 2004. Therefore, the Company will continue to operate on these TFLs according to its existing operating plans for 2004. In addition, while provisions for compensation have been made by the provincial government, the specifics will not be communicated until the areas have been identified. This takeback is not expected to have a material effect on TimberWest. The takeback on TFL 46 will not affect the pending sale of this Crown tenure.

The Private Managed Forest Land Act came into effect on November 6, 2003, replacing the Forest Land Reserve Act and the Private Land Forest Practices Regulation that, since their introduction in April 2000, had regulated managed forest land. These regulations apply to lands within the forest land reserve, including TimberWest's private lands classified as Managed Forests, and effectively cover most of TimberWest's private lands. In addition to reforestation standards, these regulations set out protection standards for four key public environmental values: clean water; protection of fish habitat; soil conservation; and protection of critical wildlife habitat.

TimberWest focuses on providing its forest workers and supervisors with the knowledge and skills they require in order to carry out their daily tasks in full compliance with the Forest Practices Code, the Forest and Range Practices Act and the Private Managed Forest Land Act.

The recent changes made by the government of British Columbia to the regulatory framework for both Crown and private timberlands could influence the Company's harvesting costs and affect the Company's access to merchantable timber on both its Crown timber tenures and its private timberlands.

TimberWest is subject to numerous and increasingly stringent environmental laws and regulations of general application relating to air emissions, effluent discharges, groundwater quality, plant and wildlife protection, employee health and safety, and waste management. Changes to these laws or regulations, or the implementation of new laws or regulations, could result in additional expenses, capital expenditures and restrictions, and delays in the Company's activities. In addition, if the Company fails to comply with applicable legislation and regulations, its operations could be interrupted and it could be subject to significant liabilities, including fines and other penalties, or required to take remedial actions, any of which could entail significant expenditures.

TimberWest employs an environmental management system to ensure the Company's operations are in compliance with these regulations. On November 29, 1999, TimberWest was awarded the ISO 14001 registration on all of its operations, which indicates that TimberWest's operations have appropriate systems in place to provide substantial compliance with applicable environmental laws. TimberWest has now been in good standing with this certification program for over four years. In December 2000, TimberWest became the first Canadian company to achieve sustainable forest management certification for its forestry operations on private land under the American Forest and Paper Association's Sustainable Forestry Initiative (SFI®). The SFI program is a rigorous system of environmental and conservation practices that includes requirements for wildlife protection, biodiversity conservation, harvesting practices and a wide range of other forest management goals. TimberWest has now been in good standing with this certification program for over three years.

Currency Risk

TimberWest sells a substantial volume of products outside of Canada (51% of gross sales in 2003), mostly in US dollars. As such, the relative strength of the Canadian dollar vs. its US counterpart has an effect on the Company's sales and earnings. The sensitivity of TimberWest's operating results to fluctuations in the value of the Canadian dollar relative to the US dollar has been discussed previously under "Results of Operations" in this management's discussion and analysis.

UNCERTAINTIES

Market Access

During 2003, TimberWest sold 1,306.0 thousand m^3 of logs into markets in Asia and the US West Coast at an average sales price premium of \$28 per m^3 over domestic sales prices. As a result, price premiums on international log shipments constitute a significant component of TimberWest's distributable cash.

Federal log export restrictions currently limit the sale of logs harvested from private lands in British Columbia into international markets. To be eligible for export, these logs must be surplus to the requirements of the domestic market. All logs sold in the domestic market, even those suitable for export, are sold at domestic prices. These restrictions limit TimberWest's ability to sell into international markets and hence limit the Company's access to the additional price premiums available in these markets. Without access to international markets, TimberWest's operations, employment levels and distributable cash would be negatively affected.

In an effort to remedy these discriminatory restrictions, in July 2001, TimberWest filed a statement of claim in the Federal Court of Canada challenging the validity of the private land log export restrictions that apply only to British Columbia, seeking a declaration that the provisions are of no force and effect. By filing this statement of claim, TimberWest is seeking fair treatment for British Columbia's private forest landowners and the implementation of a uniform, nationwide treatment for private forest landowners based on sound public policy.

Labour Relations

TimberWest employs a unionized workforce. Strikes or lockouts at the Company's or its customers' operations could restrict the Company's ability to carry on its business. At December 31, 2003, the Company had four collective agreements in place that cover all of its unionized employees.

The Industrial, Wood & Allied Workers of Canada Collective Agreement

The Industrial, Wood & Allied Workers of Canada (IWA) is the certified bargaining agent for TimberWest's hourly employees at Company operations, other than those employed at the Elk Falls Lumbermill and at Stuart Channel Wharves. TimberWest is a member of Forest Industrial Relations, which negotiates a master agreement with coastal IWA locals on behalf of industry members. The collective agreement with IWA expired on June 14, 2003.

On November 6, 2003, IWA members with coastal employers staged a one-day walkout, which was followed by a general strike that commenced November 21, 2003, and ended on December 16, 2003, when the British Columbia government legislated an end to the labour dispute. A binding mediation/arbitration process is presently underway with a deadline of May 31, 2004.

The Communications, Energy & Paperworkers Collective Agreement

The Communications, Energy and Paperworkers (CEP) is the certified bargaining agent for TimberWest's hourly employees at the Elk Falls Lumbermill. A collective agreement signed with the CEP in May 2001 specified annual salary increases of 2% for 2001 and 2002. For 2003, 2004 and 2005, salary increases are to be equal to any general increase negotiated by the coast lumber industry of British Columbia. This contract expires on May 1, 2006.

The International Longshore & Warehouse Union — Canada Collective Agreements

The International Longshore & Warehouse Union — Canada (ILWU) is the certified bargaining agent for hourly employees at TimberWest's Stuart Channel Wharves operation. TimberWest is a member of the British Columbia Maritime Employers Association and the Waterfront Foreman Employers Association. Each of these associations negotiates a master agreement with ILWU locals on behalf of industry members. Collective agreements signed in January 2003 with the ILWU provide for average annual wage increases of 2.6% over the term of the agreement, which expires on March 31, 2007.

Crown Timber Tenures

Under the Forest Act (British Columbia), allowable annual cuts on Crown timber tenures are subject to review by the Chief Forester of British Columbia every five years. The last review was completed in 2003 and resulted in a net increase in TimberWest's overall allowable annual cut. The provincial government of British Columbia has announced that it intends to implement a market-based pricing system on the coast effective February 29, 2004. The system will base rates paid by licensees for timber on the price achieved for similar timber when sold by the government through competitive auction. Stumpage rates determined for licensees will then be adjusted every quarter on the quarter to trend the market pricing of logs. For TimberWest's Crown tenures, the effect is expected to be mixed, with increased stumpage in some areas and reduced stumpage in others.

The provincial government has also made changes to cut control, appurtenancy and tenure transfers — these changes are expected to provide TimberWest greater flexibility in the management of its Crown timber tenures. Another issue of note pertaining to the Company's Crown tenures is the January 2003 announcement by the Province of British Columbia of the offer of a timber sale licence to the Ditidaht and Pacheedaht First Nations for 300,000 m^3 of timber to be harvested over a 10-year period from TimberWest's TFL 46. For the period 1993 to 1997, TimberWest cut less than its full allowable annual cut on TFL 46. TimberWest lost its right to the undercut volume for this cut control period, allowing the government to dispose of it to First Nations as part of an economic development initiative. An operating area has been established within TFL 46 where this allotment will be harvested. The effect on TimberWest of this allocation is expected to be minor as this timber sale licence award is for a historical undercut; the Company's allowable annual harvest levels remain unchanged as a result. As noted previously in this management's discussion and analysis, in September 2003, TimberWest initiated an auction process for the sale of TFL 46 and associated forest licences, and in early 2004, signed definitive agreements for the sale of these assets.

Aboriginal Land Claims

Canadian courts have recognized that aboriginal peoples may possess rights at law in respect of land used or occupied by their ancestors where treaties have not been concluded to deal with these rights. These rights may vary from limited rights of use for traditional purposes to a right of aboriginal title and will depend upon, among other things, the nature and extent of the prior aboriginal use and occupation. The courts have encouraged the Canadian federal and provincial governments and aboriginal peoples to resolve rights claims through the negotiation of treaties.

Aboriginal groups in British Columbia have claimed substantial portions of land in the province over which they claim aboriginal title or in which they have a traditional interest and for which they are seeking compensation from various levels of government. A process is now in place within British Columbia to deal with aboriginal land claims. These negotiations will be ongoing for a number of years, depending on the commitment of the parties involved and the precedents set by the outcomes of the first settlement agreements.

Under evolving jurisprudence, Canadian governments have a duty, and the Company could have a duty, to consult with aboriginal groups where the rights of aboriginal peoples may be affected.

The Company cannot predict whether aboriginal land claims or other rights in British Columbia will affect its existing Crown timber tenures, its private timberlands, its ability to harvest timber from these sources in the future or its ability to renew or secure other sources in the future.

Softwood Lumber Dispute

On May 22, 2002, the US Department of Commerce imposed countervailing duties of 18.8% against Canadian softwood lumber exports to the US. Also on May 22, 2002, the US Department of Commerce imposed anti-dumping duties, which for TimberWest have been set at 8.4%.

The Department of Commerce found that producers/exporters of softwood lumber from Canada have sold certain products below fair market value. The Canadian federal and provincial governments have launched challenges of these tariffs under the North American Free Trade Agreement and with the World Trade Organization. These US trade measures have affected the Company's domestic log customers and will continue to have an effect on softwood lumber producers in British Columbia, including the Company's ability to export softwood lumber from the Elk Falls Lumbermill. It is uncertain when this softwood lumber dispute will be resolved.

Lumber sales by TimberWest into the US were not significant during 2003. Approximately US$0.5 million of combined countervailing and anti-dumping duties on softwood lumber shipments to the US have been reflected in the Company's financial results for the year ended December 31, 2003. Cash payments for both the countervailing and anti-dumping duties have been made at the assessed rates.

Pension Valuation

In recent years, TimberWest has had the benefit of being on a contribution holiday with respect to its pension plans. The Company will complete its triennial valuation of its pension obligations during the 2004 fiscal year, effective January 1, 2004, and this valuation will be the basis for determining the amount of any funding required in the future. Despite weak performance of the capital markets over the valuation period, TimberWest has no material valuation concerns at this time. Though TimberWest remained on a contribution holiday for 2003, going forward, the Company expects a

solvency deficit to exist and, for 2004, expects to be required to fund annual service costs of approximately \$1.5 million, plus approximately \$3.0 million to fund the plans' deficit.

Legal Issues

In 1995, the British Columbia provincial government unilaterally replaced royalty fees charged on timber licences with more onerous stumpage fees. TimberWest has commenced legal action to recover compensation for the resulting loss and damage to its commercial and economic interests and investment in the timber licences. An independent study conducted for the British Columbia provincial government estimated the effect of the change in policy upon TimberWest at \$39.0 million, and TimberWest's action seeks to recover all losses. Subsequent to the commencement of the Company's legal action, claims filed by two other forest products companies on this same matter have been joined to TimberWest's suit. This claim was expected to proceed to trial in early 2004. In late 2003, the provincial government passed legislation that retroactively denies compensation to tenure holders affected by the change from royalty to stumpage fees. TimberWest is in the process of exploring its alternatives in light of this recent development.

The Company is subject to legal proceedings and claims that arise in the ordinary course of its business. Although there can be no assurance as to the disposition of these matters and the proceedings, it is the opinion of the Company's management, based upon the information available at this time, that the expected outcome of these matters, individually or in aggregate, will not have a material adverse effect on the results of operations and financial condition of the Company.

OUTLOOK

TimberWest begins 2004 with a mixed set of business conditions. On the one hand, some improvements in our end markets are emerging and there is a strong organizational commitment to Operations Excellence; on the other, there are still unresolved policy and labour issues to contend with, which adds uncertainty to the business.

In Japan, economic reports indicate that a recovery is in progress, with measures to reinforce the banking system showing results and the export sector improving. In TimberWest's markets in Japan, demand for logs and lumber is improving as log and lumber inventories are low. Higher demand is causing pricing to increase in our domestic whitewood sawlog and Japan grade log sorts. Log supply on the coast of British Columbia is tight, which is expected to also help buoy pricing through the first part of the year, especially in our log mix for Japan.

In the US market, housing starts remain strong and lumber prices are stable. While tight supply in the US Pacific Northwest is also putting upward pressure on prices, TimberWest anticipates that it will be difficult to participate fully in this market in the near term because whitewood sorts suitable for the US market are in short supply and as such the Company's exports to this market are being constrained by Notice 102. The strength of the Canadian dollar continues to be a concern in this market, but the recent weakening in the Canadian dollar against the US dollar will bring some relief.

The organization continues to work hard to reduce costs, and plans are well underway to continue with the Operations Excellence strategy in 2004. The Company also anticipates returning to more normal capital expenditure levels.

With respect to the broader business issues, TimberWest continues to support the provincial government's policy direction, particularly the implementation of a market-based stumpage system. These changes will add value to the industry on the coast and add certainty and stability for the future of the industry. However, in the near term, some coastal British Columbia sawmills will continue to force TimberWest to sell more logs at below market prices — a situation facilitated by federal government regulations that restrict the freedom of private forest landowners. The labour mediation/arbitration process is well underway for a new Coast Master Agreement and TimberWest's expectation is that a resolution to the labour agreement, too, will bring more certainty to the business climate here. The effects of both of these initiatives will become clearer in the first half of 2004.

At this point TimberWest has plans in place, even with the current uncertainty in the business climate, to meet its distribution requirements for 2004. In comparison to 2003, these plans anticipate relatively flat pricing, further cost reduction, a better end-use sort mix and a return to more normal capital expenditure levels. Our expectation is that, with these improvements, the Company's cash from operations will more closely match its distributable cash requirements for the year, and that the proceeds from the TFL 46 sale will generate cash above our distribution requirements, thereby improving our overall debt position while meeting unitholder expectations.

The Company believes that 2004 will be a year of transition and restructuring in our industry on the coast and in our Company to improve business conditions for the future. Successful implementation of plans developed for 2004 — to further reduce costs and simplify our business model — is expected to improve earnings and cash from operations in 2005.

The statements that are not historical facts contained in this report are forward-looking statements that involve risks and uncertainties. TimberWest's actual results could differ materially from those expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, general economic conditions, variations in TimberWest's product prices and changes in commodity prices generally, changes in market conditions, actions of competitors, interest rate and foreign currency fluctuations, regulatory and harvesting fee changes and other actions by governmental authorities, the ability to implement business strategies and pursue business opportunities, labour relations, weather conditions, forest fires and other natural phenomena, and other risks and uncertainties.

MANAGEMENT'S RESPONSIBILITY

To the Unitholders of TimberWest Forest Corp.:

The accompanying consolidated financial statements of TimberWest Forest Corp. and all information in this annual report are the responsibility of management and have been reviewed and approved by the Company's Board of Directors. These consolidated financial statements and related notes have been prepared by management in conformity with accounting principles generally accepted in Canada and necessarily include amounts based on management's informed judgments and estimates. Financial information included elsewhere in this annual report is consistent with that contained in the consolidated financial statements.

To assist management in fulfilling its responsibilities, a system of internal accounting controls has been established to provide reasonable assurance that the consolidated financial statements are accurate and reliable and that assets are safeguarded. Management believes that this system of internal controls has operated effectively for the year ended December 31, 2003.

KPMG LLP, Chartered Accountants, appointed by the unitholders, have audited the consolidated financial statements and conducted a review of internal accounting policies and procedures to the extent required by generally accepted auditing standards in Canada and performed such tests as they deemed necessary to enable them to express an opinion on the consolidated financial statements.

The Board of Directors, through its Audit Committee, is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls, and is ultimately responsible for reviewing and approving the consolidated financial statements and the management's discussion and analysis. The Audit Committee is composed of four independent directors who are not employees of the Company. The Audit Committee meets regularly with management, KPMG LLP and the internal auditors to review their activities and to discuss internal controls, accounting, auditing and financial matters. The Audit Committee recommends the appointment of the external auditors. The Audit Committee also meets quarterly to review interim financial statements and reports its findings to the Board of Directors for its consideration in approving the consolidated interim and annual financial statements for public dissemination.

Paul J. McElligott
President and
Chief Executive Officer

Beverlee F. Park
Vice-President, Finance, and
Chief Financial Officer

TimberWest Forest Corp.
Vancouver, Canada
January 21, 2004

AUDITORS' REPORT

To the Unitholders of TimberWest Forest Corp.:

We have audited the consolidated balance sheets of TimberWest Forest Corp. as at December 31, 2003 and 2002, and the consolidated statements of operations, cash flows and unitholders' equity for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles. As required by the Company Act (British Columbia), we report that, in our opinion, these principles have been applied, after giving effect to the change in accounting for and reporting of stock-based compensation and other stock-based payments as explained in note 3 to the financial statements, on a consistent basis.

KPMG LLP

Chartered Accountants
Vancouver, Canada
January 21, 2004

CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2003 and 2002

Consolidated Statements of Operations

(in millions of dollars, except per common share amounts)	2003	2002
Net sales	$ 428.5	$ 464.9
Operating costs and expenses:		
Cost of products sold	346.5	340.1
Depreciation, depletion and amortization	9.8	11.5
Selling, administrative and other	13.5	14.0
	369.8	365.6
Operating earnings	58.7	99.3
Interest expense	16.0	15.3
Amortization of debt issue costs	1.4	3.7
Other income	(1.8)	(0.9)
Loss on bond lock transaction	–	5.0
Restructuring charge	–	9.8
Earnings before income taxes	43.1	66.4
Income tax expense (note 11)	18.3	27.1
Net earnings	$ 24.8	$ 39.3
Basic and diluted loss per common share (note 10)	$ (0.52)	$ (0.21)

See accompanying notes to consolidated financial statements.

Consolidated Balance Sheets

(in millions of dollars)	2003	2002
Assets		
Current assets:		
Cash	$ –	$ 1.0
Accounts receivable	15.4	25.1
Inventories (note 4)	45.7	67.3
Prepaid expenses and other current assets	6.4	4.8
Future income taxes (note 11)	2.6	4.1
	70.1	102.3
Property, plant and equipment, net (note 5)	1,356.5	1,355.6
Other assets (note 6)	14.3	20.4
	$ 1,440.9	$ 1,478.3
Liabilities and Unitholders' Equity		
Current liabilities:		
Revolving credit facilities (note 7)	$ 60.0	$ –
Debentures (note 8)	–	106.5
Accounts payable and accrued liabilities	29.5	46.0
Distribution payable	20.5	20.5
	110.0	173.0
Debentures (note 8)	195.0	130.0
Long-term silviculture liability	4.6	4.8
Non-pension post-retirement benefits (note 12)	25.3	23.7
Future income taxes (note 11)	230.5	232.0
	565.4	563.5
Unitholders' equity:		
Stapled Units, consisting of Series A Subordinate Notes, preferred shares and common shares (note 9(b))	870.6	870.1
Contributed surplus	0.2	0.1
Retained earnings	4.7	44.6
	875.5	914.8
	$ 1,440.9	$ 1,478.3

Commitments and contingencies (note 16)
Subsequent event (note 19)

See accompanying notes to consolidated financial statements.

Approved on behalf of the Board:

Paul J. McElligott
Director

V. E. Daughney

V. Edward Daughney
Director

Consolidated Statements of Cash Flows

(in millions of dollars)	2003	2002
Cash provided by (used in):		
Operating activities:		
Earnings before income taxes	$ 43.1	$ 66.4
Cash income taxes (note 11)	(0.9)	(0.6)
	42.2	65.8
Items not involving cash:		
Depreciation, depletion and amortization	11.2	15.2
Gain on sale of property, plant and equipment	(3.7)	(3.9)
Other non-cash items	1.6	0.9
	51.3	78.0
Changes in non-cash working capital:		
Accounts receivable	9.7	7.0
Inventories	21.6	(13.1)
Prepaid expenses and other current assets	(1.6)	(2.5)
Accounts payable and accrued liabilities	(16.5)	4.8
	64.5	74.2
Financing activities:		
Distributions paid to unitholders	(82.1)	(78.9)
Issuance of Stapled Units on exercise of options	0.5	3.1
Issuance of Stapled Units, net	–	136.1
Forfeited distribution equivalent awards	–	0.1
Issuance of 7% debentures	65.8	129.4
Redemption of 6.5% debentures	(106.5)	–
Purchase for cancellation of 6.5% debentures	–	(18.5)
Revolving credit facility	60.0	(50.0)
Overdraft facility	–	(3.6)
Non-revolving credit facility	–	(200.0)
Deferred debt issue costs	(1.4)	(1.6)
	(63.7)	(83.9)
Investing activities:		
Proceeds from sale of property, plant and equipment	11.4	17.5
Additions to property, plant and equipment	(18.0)	(11.5)
Other assets	4.8	4.7
	(1.8)	10.7
Increase (decrease) in cash	(1.0)	1.0
Cash, beginning of year	1.0	–
Cash, end of year	$ –	$ 1.0
Supplementary information:		
Interest paid	$ 18.0	$ 17.9
Income taxes paid	$ 0.9	$ 0.9

See accompanying notes to consolidated financial statements.

Consolidated Statements of Unitholders' Equity

(in millions of dollars)	Stapled Units (note 9)				
	Number	Amount	Contributed surplus	Retained earnings	Total unitholders' equity
Balance, December 31, 2001	64,690,867	$ 728.1	$ –	$ 60.4	$ 788.5
Year ended December 31, 2002:					
Issuance of Stapled Units on close of public equity offering	11,190,650	138.9	–	–	138.9
Issuance of Stapled Units on exercise of options	311,291	3.1	–	–	3.1
Forfeited distribution equivalent awards	–	–	0.1	–	0.1
Purchase of Stapled Units for return to treasury	(20)	–	–	–	–
Net earnings	–	–	–	39.3	39.3
Interest on Series A Subordinate Notes	–	–	–	(81.8)	(81.8)
Income tax benefit thereon (note 11)	–	–	–	26.7	26.7
Balance, December 31, 2002	76,192,788	870.1	0.1	44.6	914.8
Year ended December 31, 2003:					
Issuance of Stapled Units on exercise of options	53,334	0.5	–	–	0.5
Stapled Unit option awards	–	–	0.1	–	0.1
Net earnings	–	–	–	24.8	24.8
Interest on Series A Subordinate Notes	–	–	–	(82.1)	(82.1)
Income tax benefit thereon (note 11)	–	–	–	17.4	17.4
Balance, December 31, 2003	76,246,122	$ 870.6	$ 0.2	$ 4.7	$ 875.5

See accompanying notes to consolidated financial statements.

1. Primary business activity

TimberWest Forest Corp. is incorporated under the Company Act (British Columbia) and operates in the solid wood segment of the forest industry, primarily in the harvesting and sale of logs from the coastal region of British Columbia.

2. Significant accounting policies

The accompanying consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada (GAAP).

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the period, the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements. On an ongoing basis, management reviews its estimates, including those related to litigation, environmental liabilities, inventory valuations, rates for depreciation, depletion and amortization, silviculture liabilities, income tax assets and liabilities, and pension and post-retirement obligations based on currently available information. Actual results could differ from these estimates.

In these financial statements, the term "Company" is used to mean TimberWest Forest Corp. and, where the context of the narrative permits or requires, its subsidiaries.

(a) Basis of presentation:

These consolidated financial statements include the accounts of the Company and all of its subsidiaries. All significant intercompany transactions and balances have been eliminated.

(b) Revenue recognition:

The Company recognizes its revenues when the significant risks and rewards of ownership are transferred, which is generally at time of shipment, but taking into account the FOB point.

(c) Inventories:

Inventories other than supplies are recorded at the lower of average cost and net realizable value. Supplies are recorded at cost.

(d) Property, plant and equipment:

Property, plant and equipment are capitalized at cost. Plant and equipment are depreciated on a straight-line basis at rates that reflect estimates of the economic lives of the assets based on the following annual rates of depreciation:

Assets	Rate
Buildings	2.5%–5%
Machinery and equipment	5%–25%
Other	3%–20%

Crown timber tenures are depleted in a systematic manner based on the utilization of the timber resources. Logging roads are amortized on a straight-line basis over 12 years, which approximates the utilization of the related timber resources.

Private timberlands are accounted for using the sustained yield method. Depletion will be taken on the capital cost of the private timberlands if harvest levels exceed growth on a sustained basis. Yield analyses are conducted at least every five years on all private timberlands to determine if a depletion charge is required.

Silviculture costs relating to the reforestation of private timberlands, including site preparation and planting, are expensed as incurred.

2. Significant accounting policies *(continued)*

(e) Silviculture costs:

British Columbia legislation requires the holders of Crown timber harvesting licences to assume the cost of reforestation on these licences. Accordingly, the Company records the estimated cost of reforestation of these licence areas as the timber is harvested. The portion of this liability representing expenditures projected to take place within the next year is classified as a current liability and the remainder is classified as a long-term liability.

(f) Deferred debt issue costs:

Debt issue costs related to credit facilities and debentures are deferred and amortized over the respective terms to maturity.

(g) Employee future benefits:

The Company has established employee benefit plans as described in note 12. The Company accrues its obligations under these plans and the related costs, net of plan assets. The cost of pensions and other retirement benefits earned by employees is actuarially determined using the projected benefit method prorated on service and management's best estimate of expected plan investment performance, salary escalation, retirement ages of employees and expected health-care costs. For the purpose of calculating the expected return of plan assets, those assets are valued at fair value. The excess of the net actuarial gain (loss) over 10% of the greater of the benefit obligation and the fair value of plan assets is amortized over the average remaining service period of active employees. Defined contribution plan accounting is applied to a multi-employer defined benefit plan.

(h) Series A Subordinate Notes:

As the Company may elect to pay interest on the Series A Subordinate Notes held by unitholders in common or preferred shares of the Company and may elect to pay the principal amount of the Series A Subordinate Notes held by unitholders in common shares of the Company, the $684.6 million (2002 — $684.1 million) principal amount of the Series A Subordinate Notes held by unitholders at December 31, 2003, has been classified as equity for accounting purposes, and interest thereon, on an after-tax basis, is charged directly to retained earnings as a distribution.

The aggregate annual amount of interest payable on Series A Subordinate Notes held by unitholders at December 31, 2003, is $82.2 million (2002 — $82.1 million).

(i) Foreign currency transactions:

Monetary assets and liabilities denominated in foreign currencies are translated at the period-end exchange rates. Gains or losses on translation of current assets and current liabilities are reflected in net earnings for the period. Revenues and expense items denominated in foreign currencies are translated at rates of exchange prevailing during the period.

(j) Stock-based compensation plans:

The Company has established stock-based compensation plans for eligible directors, officers and employees as described in note 13. As described in note 3, the Company's stock-based compensation plans are accounted for using the fair value–based method, and accordingly a compensation expense is recognized for awards made under these plans, including when Stapled Units or Stapled Unit options are issued to plan participants and when payments are made in connection with the Distribution Equivalent Plan. Any consideration paid by plan participants on the exercise of Stapled Unit options is credited to unitholders' equity. A credit to contributed surplus is recorded for the fair value of Stapled Unit option awards granted and for forfeited distribution equivalent awards.

(k) Earnings per share:

Earnings per share amounts are determined using the weighted average number of common shares outstanding during the year. The Company uses the treasury stock method for determining the dilutive effect of Stapled Unit options and other dilutive instruments, when applicable. Under this method, only "in the money" dilutive instruments are considered in the diluted calculations.

In millions of dollars, except per common share and per Stapled Unit amounts

3. Change in accounting policy

(a) Stock-based compensation and other stock-based payments:

Effective January 1, 2003, the Company changed its policy of accounting for Stapled Unit option awards in accordance with the recommendations of the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3870 — *Stock-based Compensation and Other Stock-based Payments.* Section 3870 establishes standards for the recognition, measurement and disclosure of stock-based compensation and other stock-based payments made in exchange for goods and services provided by employees and non-employees. It applies to transactions in which common shares, stock options or other equity instruments are granted or liabilities incurred based on the price of common shares or other equity instruments.

In fiscal 2002, the Company adopted the recommendations of Section 3870 in effect at that time and elected to continue with its previously established policy that no compensation cost was recorded on the grant of Stapled Unit options to directors, officers or employees who are in active service or employment of the Company or of any of its subsidiaries. The Company also complied with the requirement to provide additional disclosure of the effect of stock-based awards on net income and earnings per Stapled Unit on a pro forma basis.

During 2003, Section 3870 was amended to require recognition of expenses for all employee stock-based compensation transactions, including awards of Stapled Unit options, for fiscal years beginning on or after January 1, 2004. The Company made the decision to early-adopt the amendments to Section 3870 and effective January 1, 2003, has recognized a stock-based compensation expense using the fair value method for all employee stock-based compensation transactions, including awards of Stapled Unit options entered into on or after January 1, 2003. The Company has elected to adopt the recommendations of Section 3870 on a prospective basis and has not applied the fair value–based method of accounting to Stapled Unit options granted between January 1, 2002, and December 31, 2002.

(b) Cash flow and other per share information:

Effective June 30, 2003, the Company adopted the recommendations of the CICA Handbook Section 1540 — *Cash Flow Statements* and Section 3500 — *Earnings per Share.* Section 1540 and Section 3500 were amended during 2003, prohibiting the presentation of cash flow information on a per share basis in the financial statements, except for dividends or similar distributions in cash, paid or payable, to shareholders or unitholders.

In compliance with the amendments to Section 1540 and Section 3500, the Company will no longer be including separate statements of distributable cash as part of its financial statements. In addition, the Company will no longer be disclosing earnings information for the components of its equity instrument, the Stapled Unit, in its financial statements other than earnings attributable to the common share component on a per common share basis.

4. Inventories

	2003	2002
Logs	$ 41.1	$ 57.0
Lumber	3.1	8.5
Supplies	1.5	1.8
	$ 45.7	$ 67.3

In millions of dollars, except per common share and per Stapled Unit amounts

5. Property, plant and equipment

2003	Cost	Accumulated depreciation	Net book value
Logging buildings and equipment	$ 17.7	$ 2.7	$ 15.0
Lumbermill and other equipment and facilities	45.0	15.7	29.3
Land	37.7	–	37.7
	$ 100.4	$ 18.4	82.0
Timberlands (including $1,218.4 million of private timberlands) and logging roads (net of depletion and amortization)			1,274.5
			$ 1,356.5

2002	Cost	Accumulated depreciation	Net book value
Logging buildings and equipment	$ 26.8	$ 10.7	$ 16.1
Lumbermill and other equipment and facilities	35.8	13.5	22.3
Land	40.8	–	40.8
	$ 103.4	$ 24.2	79.2
Timberlands (including $1,218.4 million of private timberlands) and logging roads (net of depletion and amortization)			1,276.4
			$ 1,355.6

The $1,218.4 million (2002 — $1,218.4 million) carrying value for private timberlands includes a valuation increase adjustment of $390.8 million (2002 — $390.8 million) recorded in the year ended December 31, 2000, resulting from the adoption of Section 3465 — *Income Taxes* of the CICA Handbook, which was mandatory for fiscal years ending on or after January 1, 2000.

6. Other assets

	2003	2002
Prepaid pension benefits (note 12)	$ 7.4	$ 10.3
Deferred debt issue costs	2.8	3.3
Receivable on sale of property, plant and equipment	1.2	2.6
Other	2.9	4.2
	$ 14.3	$ 20.4

In millions of dollars, except per common share and per Stapled Unit amounts

7. Credit facilities

During 2003, the Company obtained short-term financing for $80.0 million, comprised of two $40.0 million unsecured 364-day committed revolving facilities from separate Canadian banks, and completed a two-year extension to its $125.0 million unsecured revolving facility.

As at December 31, 2003, the Company's revolving credit facilities were comprised of:

(a) $40.0 million unsecured 364-day committed revolving facility:
The Company has an unsecured 364-day committed revolving facility of $40.0 million. Under this facility, funds are available to the Company in both Canadian and US dollars by way of adjusted prime rate–based loans, Canadian dollar bankers' acceptances and letters of credit or guarantee. This facility has been underwritten by a Canadian chartered bank and is due on March 1, 2004. As at December 31, 2003, the Company had borrowings of $20.0 million on this facility. The average effective interest rate on this facility for the period it was outstanding during 2003 was 4.4%.

(b) $40.0 million unsecured 364-day committed revolving facility:
The Company has a second unsecured 364-day committed revolving facility of $40.0 million. Under this facility, funds are available to the Company in both Canadian and US dollars by way of prime rate–based loans, LIBOR loans, Canadian dollar bankers' acceptances and letters of credit or guarantee. This facility has been underwritten by a Canadian chartered bank and is due on May 26, 2004. As at December 31, 2003, the Company had borrowings of $40.0 million on this facility. The average effective interest rate on this facility for the period it was outstanding during 2003 was 4.2%.

(c) $125.0 million unsecured revolving facility:
The Company has an unsecured revolving facility of $125.0 million. Under this facility, funds are available to the Company in both Canadian and US dollars by way of adjusted prime rate–based loans, bankers' acceptances, US base rate–based loans, LIBOR loans and letters of credit or guarantee. This facility has been co-underwritten by two Canadian chartered banks and is due on June 30, 2006. As at December 31, 2003, the Company had no borrowings on this facility (2002 — nil). The average effective interest rate on this facility during 2003 was 4.9% (2002 — 4.4%).

8. Debentures

	Maturity	2003	2002
7.0% debentures	October 1, 2007	$ 195.0	$ 130.0
6.5% debentures	March 3, 2003	–	106.5
		195.0	236.5
Less: due within one year		–	(106.5)
		$ 195.0	$ 130.0

The Company's debentures are unsecured and unsubordinated and rank senior in priority to the Series A Subordinate Notes held by unitholders and equally with indebtedness of the Company under its credit facilities.

During the year ended December 31, 2003, the Company retired $106.5 million aggregate principal amount of its 6.5% debentures when they matured on March 3, 2003.

On September 26, 2003, the Company added on to its existing debenture issue by closing a public offering of $65.0 million aggregate principal amount of 7.0% unsecured senior debentures due October 1, 2007. The debentures were sold at 101.28% of their principal amount, with net proceeds to the Company of $64.4 million. The Company also received accrued interest on the debentures from April 1, 2003, of $2.2 million.

In millions of dollars, except per common share and per Stapled Unit amounts

9. Stapled Units

(a) Authorized share capital:

10,069,608,359	common shares without par value
1,600,000	class A preferred shares with a par value of $1.00 each
5,000,000,000	class B preferred shares without par value, of which the following have been designated in series:
	32,500,000 series A preferred shares
	16,000,000 series B preferred shares
	1,539,000 series C preferred shares
	65,840,000 series D preferred shares
10,000,000,000	preferred shares with a par value of $0.024456 each

(b) Stapled Units:

The Company issues equity by way of Stapled Units, each Stapled Unit consisting of approximately $8.98 face amount of Series A Subordinate Notes, 100 preferred shares and one common share. The securities comprising a Stapled Unit trade together as Stapled Units and cannot be transferred except with each other as part of a Stapled Unit until the date of maturity of the Series A Subordinate Notes or the payment of the principal amount of the Series A Subordinate Notes following an event of default and expiration of a remedies blockage period.

During the year ended December 31, 2003, the Company issued 53,334 Stapled Units (2002 — 311,291 Stapled Units) on the exercise of Stapled Unit options.

During the year ended December 31, 2002, the Company completed a public equity offering for 11,190,650 Stapled Units at a price of $12.85 per Stapled Unit for gross proceeds of $143.8 million. Net cash proceeds received were $136.1 million after costs of $7.7 million (net costs of $4.9 million after accounting for a future income tax benefit of $2.8 million). During the year ended December 31, 2002, the Company purchased 20 Stapled Units for return to treasury.

Details as to issued and outstanding Stapled Units are as follows:

	Number of Stapled Units	Series A Subordinate Notes	Preferred shares	Common shares	Issue costs	Excess (shortfall) of stated value of Stapled Units over purchase/ issue price	Total Stapled Units
Balance, December 31, 2001	64,690,867	$ 580.8	$ 158.1	$ 14.3	$ (25.6)	$ 0.5	$ 728.1
Year ended December 31, 2002:							
Stapled Units issued on close of public equity offering	11,190,650	100.5	27.4	15.9	(4.9)	–	138.9
Stapled Unit options exercised	311,291	2.8	0.7	–	–	(0.4)	3.1
Stapled Units purchased for return to treasury	(20)	–	–	–	–	–	–
Balance, December 31, 2002	76,192,788	684.1	186.2	30.2	(30.5)	0.1	870.1
Year ended December 31, 2003:							
Stapled Unit options exercised	53,334	0.5	0.1	–	–	(0.1)	0.5
Balance, December 31, 2003	76,246,122	$ 684.6	$ 186.3	$ 30.2	$ (30.5)	$ –	$ 870.6

In millions of dollars, except per common share and per Stapled Unit amounts

9. Stapled Units *(continued)*

(b) Stapled Units *(continued)*:

Details as to each of the components of the Stapled Units are as follows:

(i) Series A Subordinate Notes (see note 2(h)):

	Number of notes	Amount
Balance, December 31, 2001	64,690,867	$ 580.8
Year ended December 31, 2002:		
Series A Subordinate Notes issued on close of public equity offering	11,190,650	100.5
Series A Subordinate Notes issued on exercise of Stapled Unit options	311,291	2.8
Series A Subordinate Notes purchased for return to treasury	(20)	–
Balance, December 31, 2002	76,192,788	684.1
Year ended December 31, 2003:		
Series A Subordinate Notes issued on exercise of Stapled Unit options	53,334	0.5
Balance, December 31, 2003	76,246,122	$ 684.6

Each Series A Subordinate Note has been issued with a face amount of $8.978806569, entitling the holder to an interest payment per unit of $1.077456788 per annum (12%).

The Series A Subordinate Notes are unsecured and subordinate to all credit facilities (see note 7) and debentures (see note 8). The principal amount of the Series A Subordinate Notes plus accrued and unpaid interest thereon are due on August 31, 2038, unless such date is extended by the Company at the time of the issuance of additional Subordinate Notes to a date not later than the earlier of: *(i)* the date of maturity of such additional Subordinate Notes; and *(ii)* August 31, 2048, and will be payable by cash or, at the option of the Company, by delivery of common shares to the Subordinate Note Trustee for the benefit of the holders of the Subordinate Notes.

(ii) Preferred shares:

	Number of shares	Amount
Balance, December 31, 2001	6,469,086,700	$ 158.1
Year ended December 31, 2002:		
Preferred shares issued on close of public equity offering	1,119,065,000	27.4
Preferred shares issued on exercise of Stapled Unit options	31,129,100	0.7
Preferred shares purchased for return to treasury	(2,000)	–
Balance, December 31, 2002	7,619,278,800	186.2
Year ended December 31, 2003:		
Preferred shares issued on exercise of Stapled Unit options	5,333,400	0.1
Balance, December 31, 2003	7,624,612,200	$ 186.3

The holders of the preferred shares are entitled to the receipt of dividends as may be declared by the Board of Directors from time to time and are not entitled to any voting rights except as may be provided under the Company Act. The preferred shares may be redeemed at the option of the Company in whole at any time or in part from time to time at the par value of $0.024456 per share.

In millions of dollars, except per common share and per Stapled Unit amounts

9. Stapled Units *(continued)*

(b) Stapled Units *(continued)*:

(iii) Common shares:

	Number of shares	Amount
Balance, December 31, 2001	64,690,867	$ 14.3
Year ended December 31, 2002:		
Common shares issued on close of public equity offering	11,190,650	15.9
Common shares issued on exercise of Stapled Unit options	311,291	–
Common shares purchased for return to treasury	(20)	–
Balance, December 31, 2002	76,192,788	30.2
Year ended December 31, 2003:		
Common shares issued on exercise of Stapled Unit options	**53,334**	–
Balance, December 31, 2003	**76,246,122**	**$ 30.2**

(c) Class B preferred shares issuable in series:

Details as to the series of class B preferred shares issued are as follows:

	Number of shares	Amount
Series A	32,500,000	$ 325.0
Series D	62,500,000	625.0
		950.0
Class B preferred shares owned by the Company's subsidiaries		(950.0)
Balance, December 31, 2003 and 2002		$ –

In millions of dollars, except per common share and per Stapled Unit amounts

10. Loss per share

	2003	2002
Net earnings	$ 24.8	$ 39.3
Less:		
Distributions on Series A Subordinate Notes	(82.1)	(81.8)
Tax benefit thereon	17.4	26.7
	(64.7)	(55.1)
Loss attributable to common shares	$ (39.9)	$ (15.8)
Basic weighted average number of common shares	76,234,486	74,686,050
Incremental common shares from potential exercise of options	74,597	121,551
Diluted weighted average number of common shares	76,309,083	74,807,601
Basic and diluted loss per common share	$ (0.52)	$ (0.21)

11. Income taxes

Income tax expense consists of:

	2003			2002		
	Statement of operations	Distributions	Total	Statement of operations	Distributions	Total
Current:						
Large corporation tax	$ 0.9	$ –	$ 0.9	$ 0.6	$ –	$ 0.6
Income tax benefit on interest on Series A Subordinate Notes charged directly to distributions	17.4	(17.4)	–	26.7	(26.7)	–
	18.3	(17.4)	0.9	27.3	(26.7)	0.6
Future:						
Future income tax recovery	–	–	–	(0.2)	–	(0.2)
Income tax expense	$ 18.3	$ (17.4)	$ 0.9	$ 27.1	$ (26.7)	$ 0.4

In millions of dollars, except per common share and per Stapled Unit amounts

11. Income taxes *(continued)*

The Company's effective income tax rate differs from the Canadian statutory income tax rate. The principal factors causing the difference are as follows:

	2003			2002		
	Statement of operations	Distributions	Total	Statement of operations	Distributions	Total
Earnings before income taxes	$ 43.1	$ –	$ 43.1	$ 66.4	$ –	$ 66.4
Interest on Series A Subordinate Notes	–	(82.1)	(82.1)	–	(81.8)	(81.8)
	$ 43.1	$ (82.1)	$ (39.0)	$ 66.4	$ (81.8)	$ (15.4)
Income tax expense (benefit) at statutory rates (2003 — 37.6%; 2002 — 39.6%)	$ 16.2	$ (30.9)	$ (14.7)	$ 26.3	$ (32.4)	$ (6.1)
Large corporation tax	0.9	–	0.9	0.6	–	0.6
Non-deductible expenses	1.2	–	1.2	0.4	–	0.4
Tax losses not recognized	–	13.5	13.5	–	5.7	5.7
Permanent difference tax effected at capital gains rate	(0.4)	–	(0.4)	(0.6)	–	(0.6)
Change in prior year estimated tax values	0.1	–	0.1	2.0	–	2.0
Other	0.3	–	0.3	(1.6)	–	(1.6)
Income tax expense	$ 18.3	$ (17.4)	$ 0.9	$ 27.1	$ (26.7)	$ 0.4

The tax effects of temporary differences that give rise to significant portions of the future tax assets and future tax liabilities at December 31, 2003 and 2002, are presented below:

	2003	2002
Net future tax assets:		
Current silviculture liability	$ 0.7	$ 0.8
Accruals for financial reporting purposes not deductible for tax purposes	1.9	3.3
Net future tax assets, current	$ 2.6	$ 4.1
Net future tax liabilities:		
Private timberlands	$ (221.5)	$ (222.3)
Other property, plant and equipment	(18.3)	(17.9)
Other assets	(1.3)	(1.9)
Non-pension post-retirement benefits	9.0	8.4
Long-term silviculture liability	1.6	1.7
Capital loss carryforwards	26.2	26.2
Non-capital loss carryforwards	49.3	35.2
Total gross future tax liabilities	(155.0)	(170.6)
Valuation allowance	(75.5)	(61.4)
Net future tax liabilities, non-current	$ (230.5)	$ (232.0)

In millions of dollars, except per common share and per Stapled Unit amounts

12. Employee benefits

The Company, through its subsidiaries, maintains pension plans that include defined benefit and defined contribution segments available to all salaried employees and to hourly employees not covered by union pension plans. The Company also provides non-pension benefits consisting of group life insurance and medical benefits to eligible retired employees, which the Company funds on an as-incurred basis.

Under the provisions of the Company's pension plans, current service contributions to both the defined benefit and defined contribution segments may be funded by an actuarial surplus in the defined benefit segment of the plan. For the year ended December 31, 2003, the Company's required contributions of $1.1 million (2002 — $1.0 million) under the defined contribution segment and its required contributions of $0.7 million (2002 — $0.6 million) under the defined benefit segment were both funded from a surplus in the defined benefit segment of the plan.

The Company will complete its triennial actuarial valuation during the 2004 fiscal year, effective January 1, 2004, and this valuation will be the basis for determining the amount of any funding required in the future.

Unionized employees of the Company's subsidiaries are members of a multi-employer defined benefit pension plan providing both pension and other retirement benefits. This plan, to which the Company contributes a pre-set amount per hour worked by an employee (aggregating $3.1 million during the year ended December 31, 2003 (2002 — $3.2 million)), is accounted for as a defined contribution plan, but the contributions are not included in the defined contribution plan expense above. The Company has no further obligations relating to the pension benefits of its unionized employees.

Information about the Company's defined benefit plans other than the multi-employer defined benefit plan, in aggregate, is as follows:

	Pension benefit plans		Post-retirement benefit plans	
	2003	2002	2003	2002
Change in accrued benefit obligation during the year:				
Accrued benefit obligation, beginning of year	$ 102.0	$ 103.8	$ 31.7	$ 25.0
Current service cost	0.7	0.6	0.5	0.4
Interest cost	6.4	6.5	2.3	1.9
Benefits paid	(9.6)	(8.9)	(1.8)	(1.6)
Net actuarial loss	4.3	–	7.2	6.0
Accrued benefit obligation, end of year	103.8	102.0	39.9	31.7
Change in plan assets during the year:				
Plan assets, fair value at beginning of year	86.0	96.2	–	–
Use of surplus for defined contribution segment service cost	(1.1)	(1.0)	–	–
Actual return on plan assets	10.1	(0.9)	–	–
Employer contributions	0.8	0.6	1.8	1.6
Benefits paid	(9.6)	(8.9)	(1.8)	(1.6)
Plan assets, fair value at end of year	86.2	86.0	–	–
Reconciliation of funded status:				
Accrued benefit obligation in excess of plan assets	(17.6)	(16.0)	(39.9)	(31.7)
Unamortized net actuarial loss	22.3	22.3	14.6	8.0
Unamortized past service costs	2.7	4.0	–	–
Net accrued benefit asset (liability)	$ 7.4	$ 10.3	$ (25.3)	$ (23.7)

In millions of dollars, except per common share and per Stapled Unit amounts

12. Employee benefits *(continued)*

Included in the accrued benefit obligation and fair value of plan assets at year end are the following amounts in respect of plans that are not fully funded:

	Pension benefit plans		Post-retirement benefit plans	
	2003	2002	2003	2002
Accrued benefit obligation	$ 10.8	$ 9.9	$ 39.9	$ 31.7
Fair value of plan assets	–	–	–	–
Net accrued benefit liability	$ (10.8)	$ (9.9)	$ (39.9)	$ (31.7)

The Company's net benefit plan expense is as follows:

	Pension benefit plans		Post-retirement benefit plans	
	2003	2002	2003	2002
Current service cost	$ 1.8	$ 1.6	$ 0.5	$ 0.4
Interest cost	6.4	6.5	2.3	1.9
Expected return on plan assets	(6.5)	(7.3)	–	–
Amortization of past service costs	1.3	1.3	–	–
Amortization of experience loss	0.7	0.3	0.6	0.4
Expense recognized in the current year	$ 3.7	$ 2.4	$ 3.4	$ 2.7

The significant actuarial assumptions adopted in measuring the Company's accrued benefit obligations are as follows (weighted-average assumptions as of December 31):

	Pension benefit plans		Post-retirement benefit plans	
	2003	2002	2003	2002
Discount rate	6.0%	6.5%	6.0%	6.5%
Expected long-term rate of return on plan assets	7.5%	8.0%	–	–
Rate of compensation increase	3.5%	4.0%	–	–

For measurement purposes, a 7% annual rate of increase in the per capita cost of covered health-care benefits was assumed for 2003 (2002 — 7%). The rate was assumed to decrease gradually to 5% for 2004 and remain at that level thereafter.

In order to retain and encourage the continuing service of its officers and key employees, the Company has entered into agreements with its officers and key employees providing a supplement to the severance entitlements to which these officers are entitled under their regular employment arrangements if employment is terminated without cause within 24 months following a change of control of the Company, as defined in the agreements.

In millions of dollars, except per common share and per Stapled Unit amounts

13. Stock-based compensation plans

(a) Stapled Unit Option Plan:

Under the Stapled Unit Option Plan established in 2000, the Company may grant options for the purchase of Stapled Units to directors, officers or employees who are in active service or employment with the Company or any of its subsidiaries. The maximum number of Stapled Units that may be issued pursuant to this plan and all options granted thereunder is limited to 3,500,000 Stapled Units. The expiry date and vesting provisions of options granted are established at the time an award is made. Options must expire within 10 years of the date of grant, and options granted generally vest in equal proportions over a period of three years. The exercise price of grants awarded may not be less than the weighted average trading price of the Stapled Units on the Toronto Stock Exchange over the five consecutive trading days immediately before the date of grant.

Activity in the Company's Stapled Unit Option Plan was as follows:

	2003		2002	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Options outstanding, beginning of year	1,314,387	$ 11.75	1,711,774	$ 11.52
Granted	267,047	11.90	55,200	13.09
Exercised	(53,334)	8.91	(311,291)	10.18
Cancelled	(9,367)	12.95	(141,296)	12.93
Options outstanding, end of year	1,518,733	$ 11.87	1,314,387	$ 11.75

A summary of Stapled Unit options outstanding at December 31, 2003, is as follows:

Total outstanding				Total exercisable	
Number of options	Exercise price	Weighted average exercise price	Weighted average years to expiration	Number of options	Weighted average exercise price
236,667	$ 8.91	$ 8.91	6.2	236,667	$ 8.91
146,209	10.71	10.71	7.1	96,209	10.71
58,340	11.67	11.67	2.8	58,340	11.67
264,467	11.90	11.90	4.1	–	–
2,580	12.28	12.28	4.2	–	–
126,000	12.72	12.72	2.9	84,000	12.72
6,000	12.79	12.79	3.7	2,000	12.79
144,600	12.84	12.84	2.9	96,399	12.84
15,000	12.87	12.87	3.1	5,000	12.87
484,670	13.03	13.03	3.0	422,538	13.03
9,000	13.13	13.13	3.3	3,000	13.13
12,500	13.14	13.14	3.4	4,167	13.14
12,700	13.41	13.41	3.4	4,233	13.41
1,518,733	$8.91 – $13.41	$ 11.87	4.0	1,012,553	$ 11.73

In millions of dollars, except per common share and per Stapled Unit amounts

13. Stock-based compensation plans *(continued)*

(a) Stapled Unit Option Plan *(continued):*

Prior to January 1, 2003, the Company's policy was that no compensation cost was recorded on stock-based compensation awards granted to employees under this plan. Effective January 1, 2003, the Company changed its policy of accounting for awards under this plan and now applies the fair value–based method of accounting for all stock-based compensation transactions (see note 3). The Company has made this change in accounting policy on a prospective basis and accordingly has not applied the fair value–based method of accounting to Stapled Unit options granted between January 1, 2002, and December 31, 2002.

The compensation cost for the 267,047 Stapled Unit options granted under the Stapled Unit Option Plan in 2003, determined using the fair value method of accounting for stock-based compensation, is $0.3 million. As this amount is amortized against income over the three-year vesting period of the underlying options, a charge of $0.1 million was recognized in net earnings for the year ended December 31, 2003, with a corresponding credit to contributed surplus.

The compensation cost for the 55,200 Stapled Unit options granted under the Stapled Unit Option Plan in 2002, determined based on their fair value at the grant date of the awards, consistent with the fair value method of accounting for stock-based compensation, would have been $0.1 million. As this amount would be amortized against income over the three-year vesting period of the underlying options, there would have been no adjustment to the Company's net earnings and earnings per common share reported for the year ended December 31, 2003 (2002 — nil).

The fair value of each option granted was estimated on the date of grant using the Black-Scholes option pricing model using the following weighted average assumptions:

	2003	2002
Risk-free interest rate	4.3%	5.7%
Expected life (years)	5.0	5.0
Expected volatility	25.3%	27.1%
Dividend yield	9.1%	8.2%
Number of options granted	267,047	55,200
Weighted average fair value of options granted	$ 1.07	$ 1.72

Consideration paid by option holders on the exercise of options is recorded as an addition to Stapled Units.

(b) Distribution Equivalent Plan:

The Distribution Equivalent Plan was introduced as a supplement to the Stapled Unit Option Plan in 2001. Under this supplemental plan, the Company awards Stapled Unit option holders an amount equal to actual distributions paid on the Company's Stapled Units. Awards granted under the Distribution Equivalent Plan vest under the same terms that apply to the corresponding options and can only be exercised at the time of exercise of the corresponding options.

The Company applies the principles of the fair value–based method of accounting for stock-based compensation to awards granted under this plan. Awards are accrued on a basis equal to actual distributions paid on the Company's issued and outstanding Stapled Units and are charged to income as the underlying Stapled Unit options vest. For the year ended December 31, 2003, $1.2 million (2002 — $1.1 million) has been accrued for awards granted under this plan and $1.1 million (2002 — $0.8 million) has been amortized against net earnings.

In millions of dollars, except per common share and per Stapled Unit amounts

14. Segment information

The Company has one reportable segment, being solid wood, identified based on the way that management organizes its business for making operating decisions and assessing performance. All of the Company's assets are located in British Columbia, Canada.

Net sales by product are as follows:

	2003	2002
Logs	$ 340.1	$ 378.2
Lumber	62.6	58.0
Wood chips and other	17.2	12.2
Real estate	8.6	16.5
	$ 428.5	$ 464.9

Net sales by geographic area are as follows:

	2003	2002
Canada	$ 209.4	$ 232.4
Japan	131.6	145.9
United States	59.0	75.2
Belgium	7.7	3.7
China	7.3	1.1
Korea	6.0	2.5
Australia	4.0	1.3
Other	3.5	2.8
	$ 428.5	$ 464.9

Revenues are attributed to geographic area based on final shipping destination.

In 2003, the Company had sales to one customer whose individual sales accounted for approximately 10% of the Company's consolidated sales. In 2002, the Company had sales to two customers whose individual sales exceeded 10% of the Company's consolidated sales, with one customer accounting for approximately 12% of consolidated sales and one customer accounting for approximately 10% of consolidated sales.

15. Financial instruments

(a) Fair values:

The carrying values of accounts receivable, accounts payable and accrued liabilities and distribution payable approximate their fair values due to the short term to maturity of these instruments.

The carrying value of the receivable on sale of assets included in other assets (see note 6) is estimated to approximate its fair value, as annual payments are received on this receivable that approximate interest at market rates.

The carrying values of drawings on available credit facilities approximate their fair values, as they bear floating interest rates that approximate market rates and have a short term to maturity.

At December 31, 2003, the Company's 7.0% debentures had a carrying value of $195.0 million (2002 — $130.0 million) and a fair value of $200.6 million (2002 — $130.7 million). The debenture fair values have been estimated based on quotes provided by financial institutions as at December 31, 2003 and 2002.

15. Financial instruments *(continued)*

(b) Credit risk:

The Company is exposed to credit risk on accounts receivable from customers. To manage its credit risk, the Company has credit policies that include the analysis of the financial position of its customers and the regular review of their credit limits. In certain offshore markets, the Company requires bank letters of credit.

16. Commitments and contingencies

(a) Operating leases:

The Company is committed to payments under operating leases for equipment and office premises through to 2011 in the total amount of approximately \$25.3 million. Annual payments over the term of these commitments are: 2004 — \$11.8 million; 2005 — \$7.5 million; 2006 — \$3.4 million; 2007 — \$1.4 million; 2008 — \$0.6 million; and 2009 and beyond — \$0.6 million.

(b) Letters of credit and guarantee:

At December 31, 2003, the Company had commitments of \$15.3 million (2002 — \$14.2 million) relating to outstanding letters of credit issued under its available credit facilities, which secure various obligations of the Company.

(c) Legal claims:

The Company is subject to legal proceedings and claims that arise in the ordinary course of its business. Although there can be no assurance as to the disposition of these matters and the proceedings, it is the opinion of the Company's management, based upon the information available at this time, that the expected outcome of these matters, individually or in aggregate, will not have a material adverse effect on the results of operations and financial condition of the Company.

17. Forestry Revitalization Plan

In March 2003, the Government of BC (the Crown) introduced its Forestry Revitalization Plan (the Plan), which has subsequently been implemented, in part, through the Forestry Revitalization Act, the Forest and Range Practices Act, and amendments to the Forest Act and Forest Practices Code of British Columbia Act. The Plan provides for significant changes to Crown forest policy and to the existing allocation of Crown timber harvesting rights to licensees. The changes in the Plan include the relaxing of cut control requirements, the elimination of appurtenancy and timber processing requirements, more flexibility to consolidate and subdivide forest tenures, increased freedom to transfer forest tenures without restriction or penalty, and a market-based stumpage system. As well, licensees, including the Company, have had their aggregate allowable annual cut attributable to Crown lands reduced by 20%, with the first 200,000 m^3 exempt from this reduction, as well as a 20% reduction in the area of Timber Licences held outside of Tree Farm Licences (TFLs). The Plan states that approximately half of this volume will be redistributed to provide opportunities for woodlots, community forests and First Nations and the other half will be made available for public auction. The Crown has acknowledged that licensees will be fairly compensated for the value of lost harvesting rights and for improvements on Crown land.

TimberWest has been advised by the Ministry of Forests that it will be subject to a 200,000 m^3 tenure takeback to be allocated such that 168,000 m^3 will be taken back from Tree Farm Licence 46 (TFL 46) and 32,000 m^3 from Tree Farm Licence 47 (TFL 47). While the total allowable annual cut has been identified for takeback, licensees have been notified that the identification of areas comprising this volume will not be completed until late 2004. Therefore, the Company will continue to operate on these TFLs according to its existing operating plans for 2004. In addition, while provisions for compensation have been made by the provincial government, the specifics will not be communicated until the areas have been identified. This takeback is not expected to have a material effect on TimberWest. The takeback on TFL 46 will not affect the pending sale of this Crown tenure (see note 19).

18. Comparative figures

Certain prior year figures have been restated to conform to the 2003 presentation.

19. Subsequent event

On January 21, 2004, the Company signed a definitive agreement for the sale of its southern Vancouver Island public land operations, referred to as TFL 46. The sale is subject to several conditions and is expected to close during the first half of 2004. Sale proceeds on this transaction are expected to exceed the carrying value of the assets being disposed of.

EXECUTIVE MANAGEMENT TEAM & BOARD OF DIRECTORS

Executive Management Team

Paul J. McElligott
President and Chief Executive Officer
North Vancouver, British Columbia

Virginia Aulin
Vice-President, Public Affairs and Government Relations
Vancouver, British Columbia

John Kelvin
Vice-President, Log Marketing and Sales
North Vancouver, British Columbia

Hamish Kerr
Vice-President, Strategic Planning and Forest Policy
West Vancouver, British Columbia

John Mann
Vice-President, Coast Timberlands
Nanaimo, British Columbia

Beverlee Park
Vice-President, Finance, and Chief Financial Officer
West Vancouver, British Columbia

Mark Stock
Vice-President, Human Resources
and Information Technology
North Vancouver, British Columbia

Ed Vervynck
General Manager, Manufacturing
Surrey, British Columbia

Gerry Young
Assistant Vice-President, Timberland Operations
Courtenay, British Columbia

Board of Directors

V. Edward Daughney[1, 2]
Chairman, TimberWest Forest Corp.,
and Principal and Chairman,
Echelon Home Products Ltd.
Vancouver, British Columbia
Director since 1997

William C. Brown[1, 3]
Corporate Director
West Vancouver, British Columbia
Director since 1997

Paul J. McElligott
President and Chief Executive Officer,
TimberWest Forest Corp.
North Vancouver, British Columbia
Director since 1997

Robert W. Murdoch[1, 2, 4]
Corporate Director
Salt Spring Island, British Columbia
Director since 2001

Anthony J. Petrina[2, 3]
Corporate Director
Vancouver, British Columbia
Director since 1997

Conrad A. Pinette[1, 3]
President and Chief Operating Officer,
Lignum Ltd.
Vancouver, British Columbia
Director since 2002

Kenneth A. Shields[2, 4]
President and Chief Executive Officer,
Raymond James Ltd.
Vancouver, British Columbia
Director since 1997

Committees of the Board
[1] Audit
[2] Governance & Human Resources
[3] Environment, Health & Safety
[4] Pension

For full descriptions of the Board committees, please see TimberWest's Information Circular.

Bios for members of the Executive Management Team and Board of Directors are available on TimberWest's web site at
http://www.timberwest.com/compinfo_directors.cfm

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ANNUAL GENERAL MEETING

The Annual General Meeting of the Unitholders will be held on Tuesday, May 11, 2004, at 2:00 p.m. (PST) at 9350 Bomber Base Road, Port Alberni, British Columbia, Canada.

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